United States District Court
Southern District of Texas

Case Number: H-06-1853

ATTACHMENT

Description: Memorandum of Law in support of Plt's Motion for preliminary injunction

☐ State Court Record ☐ State Court Record Continued

☐ Administrative Record

☐ Document continued - Part 4 of ~~8~~ 11

☐ Exhibit to: ______
number(s) / letter(s) ______

Other: ______

As seen in Business Week, August 2003

The Global Brand Scoreboard

RANK	2003 BRAND VALUE $BILLIONS	2002 BRAND VALUE $BILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
40 HEINZ	7.10	7.35	-3	U.S.	The world's favorite ketchup now comes in upside-down bottles and colors like "stellar blue." But competition took a bite.
41 GOLDMAN SACHS	7.04	7.19	-2	U.S.	Raising capital for Corporate America made it arguably the most prestigious investment bank. But a drought in mergers and equity issuances took a toll.
42 VOLKSWAGEN	6.94	7.21	-4	Germany	The stalwart maker of quality mass-market cars suffered from high costs, an aging lineup, fierce French competition, and a slew of overlapping brands.
43 IKEA	6.92	6.55	+6	Sweden	The chain made flat-packed furniture both affordable and fashionable, bringing its concept of democratic design to 31 countries.
44 HARLEY-DAVIDSON	6.78	6.27	+8	U.S.	Aging customers still think Harley when they think motorcycle. They're also rich enough to afford such innovations as the sleek $18,000 V-Rod.
45 LOUIS VUITTON	6.71	7.05	-5	France	A downturn in tourism slowed this awesome profit machine fueled by monogrammed bags and accessories.
46 MTV	6.28	6.08	+3	U.S.	Still a big favorite among teens, and not just in the U.S. MTV International was one of the fastest-growing businesses at parent Viacom Inc.
47 L'OREAL	5.60	5.08	+10	France	Who's boycotting France? Not the millions of women who made L'Oreal the No.1 cosmetics seller in the U.S.
48 XEROX	5.58	5.31	+5	U.S.	With new financing and a range of hot color products, the troubled copier company's image was on the mend.
49 KFC	5.58	5.35	+4	U.S.	The chicken chain goosed global business by promoting local fare—tempura crispy strips in Japan and potato-and-onion croquettes in Holland.
50 APPLE	5.55	5.32	+4	U.S.	The "i's" have it—iPod, iTunes, and iBooks lifted the perennial underdog, while the innovative Music Store download service left rivals in the dust.
51 PIZZA HUT	5.31	6.05	-12	U.S.	The dough wasn't rising. Asian restaurant sales were hurt by SARS, while at home the chain was slow to sling popular new products such as wings
52 ACCENTURE	5.30	5.18	+2	U.S.	Hit hard by the slump in telecom, the consulting icon took its own advice and nimbly built its outsourcing specialty.
53 GUCCI	5.10	5.30	-4	Italy	Chief designer Tom Ford was still a hit on the catwalks of Paris and New York, but Gucci's profits were shredded by economic stagnation and SARS.
54 KLEENEX	5.06	5.04	0	U.S.	From aromatherapy tissues to 3-D holiday boxes, this leader still managed to pull out some fresh ideas.
55 WRIGLEY'S	5.06	4.75	+7	U.S.	Hip ad campaigns to relaunch core brands Juicy Fruit and Doublemint and introduction of new sugar-free gum reinvigorated the chew-chew train.
56 COLGATE	4.69	4.60	+2	U.S.	As it neared the end of its second century, the brand continued to win over more smiles.
57 AVON	4.63	4.40	+5	U.S.	The Avon Ladies were on a tear, leveraging healthy R&D and marketing budgets through online sales and an expanding door-to-door network.
58 SUN MICROSYSTEMS	4.47	4.77	-6	U.S.	A perception that this computer maker wasn't keeping up with technology trends made it appear as less than cutting-edge.
59 PHILIPS	4.46	4.56	-2	Netherlands	In Europe, its name equals home electronics, but Philips struggled with awareness in the U.S. and perennially tough competition from Asia.
60 NESTLE	4.46	4.43	+1	Switzerland	From chocolate to baby formula, the Swiss food giant keeps the world's pantry stocked.
61 CHANEL	4.32	4.27	+1	France	A symbol of Parisian sophistication for mom's generation, but Chanel had a harder time luring younger customers.
62 DANONE	4.24	4.05	+5	France	The maker of Dannon yogurt, already a powerhouse in Europe, was betting big on emerging markets.
63 KRAFT	4.17	4.08	+2	U.S.	The master of line extensions scored with new frozen-pizza flavors and other products but lost share on its cheese business to private labels.
64 AOL	3.96	4.33	-8	U.S.	Often dubbed the "Internet on training wheels," the king of the dial-up services risked losing subscribers as they graduated to broadband connections.
65 YAHOO!	3.90	3.86	+1	U.S.	This Internet icon soared again but will have to watch out for the Net's next killer brand: Google.
66 TIME	3.78	3.68	+3	U.S.	After winning a National Magazine Award for coverage of September 11, the weekly ramped up again with excellent war reporting and photography.
67 ADIDAS	3.68	3.69	0	Germany	The maker of athletic shoes and clothing suffered from a plunge in U.S. sales as youths balked at paying more than $100 for a pair of sneakers.
68 ROLEX	3.67	3.69	0	Switzerland	Tough times failed to put a dent in the popularity of the signature Swiss watches.
69 BP	3.58	3.39	+6	Britain	John Browne was once again front and center with his controversial "Beyond Petroleum" campaign. A megadeal in Russia also helped.

As seen in Business Week, August 2003

The Global Brand Scoreboard

RANK	2003 BRAND VALUE $BILLIONS	2002 BRAND VALUE $BILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
70 TIFFANY	3.54	3.48	+2	U.S.	Even hard times couldn't dim the luster of Tiffany's extravagant baubles in their signature blue box.
71 DURACELL	3.44	3.41	+1	U.S.	Terrorist fears bolstered battery sales, but the category remained hampered by cutthroat competition.
72 BACARDI	3.43	3.34	+3	Bermuda	New flavors, coupled with the popularity of the mojito—a Cuban rum mint julep—kept the venerable rum brand on the hip parade.
73 HERMES	3.42	N/A	N/A	France	Known for classic scarves and leather goods, Hermes recently hired celebrity designer Jean-Paul Gaultier to update its image.
74 AMAZON.COM	3.40	3.18	+7	U.S.	Amazon's relentless focus on making online buying easier—not to mention steady progress toward profits—improved its standing among consumers.
75 CATERPILLAR	3.36	3.22	+5	U.S.	The economy gave Cat a rough ride, but the heavy-equipment and engine maker bulldozed ahead, strengthening earnings through cost-cutting.
76 REUTERS	3.30	4.61	-28	Britain	The news and data service still had not found the formula to outgun financial-screen rival Bloomberg in a weak market.
77 LEVI'S	3.30	3.45	-5	U.S.	This struggling American icon has tried—sometimes too hard—to be cool, but it's also going mass-market with a line for Wal-Mart.
78 HERTZ	3.29	3.36	-2	U.S.	Saddled with a difficult travel market, Hertz Rent-A-Car had a tough time standing out as the premium choice. This company will have to try harder.
79 PANASONIC	3.26	3.14	+4	Japan	Once a dowdy line of home electronics, Matsushita's Panasonic brand stood for style, quality, and function-packed products.
80 ERICSSON	3.15	3.59	-12	Sweden	The cellular equipment giant survived the telecom bust but faced a tough future. Two years of sturm and drang have taken a toll.
81 MOTOROLA	3.10	3.42	-9	U.S.	This electronics brand was cut down to size by intense competition and weak demand, while product delays put customers on hold.
82 HENNESSY	3.00	N/A	N/A	France	Hip-hoppers and other celebs made this top-of-the-line cognac relevant to a new generation of drinkers.
83 SHELL	2.98	2.81	+6	Brit./Nether.	CEO Phil Watts drove a money machine fueled by $30 oil prices and hard-nosed cost-cutting.
84 BOEING	2.86	2.97	-4	U.S.	Management worked hard to prove the brand stood for more than commercial airliners, only to fall behind Airbus in that crucial market.
85 SMIRNOFF	2.81	2.72	+3	Britain	Shook up the booze business with its introduction of flavored vodkas and a range of ready-to-drink Smirnoff spin-off products.
86 JOHNSON & JOHNSON	2.71	2.51	+8	U.S.	The halo effect from J&J's trusted consumer brands helped the company's sales reps as they marketed a broad lineup of drugs and devices.
87 PRADA	2.54	2.49	+2	Italy	The Italian icon's minimalist clothing, nylon handbags, and ultra-trendy shoes took fashion capitals by storm, but heavy debt slowed its strut.
88 MOET & CHANDON	2.52	2.45	+3	France	With sales up 14% last year, it kept the bubbly flowing at parent company LVMH Moet Hennessy Louis Vuitton.
89 NISSAN	2.50	N/A	N/A	Japan	On a roll under new management from Renault, but the brand's reputation had yet to catch up to Nissan's crowd-pleasing new models.
90 HEINEKEN	2.43	2.40	+1	Netherlands	Young people were drinking less, but if they spend more for quality, the Dutch-made premium beer could prosper.
91 MOBIL	2.41	2.36	+2	U.S.	Success of its reformulated Mobil 1 motor oil, racing sponsorships, and its status as NASCAR's official lubricant reinvigorated this ExxonMobil franchise.
92 NIVEA	2.22	2.06	+8	Germany	Hamburg-based parent company Beiersdorf kept the skin cream growing by spreading it into categories such as sun protection and deodorants.
93 STARBUCKS	2.14	1.96	+9	U.S.	This fast-growing brand continued to corner the U.S. market, although it hit some speed bumps overseas.
94 BURGER KING	2.12	2.16	-2	U.S.	As talks dragged on to sell the Home of the Whopper, it suffered from a stale menu, management exodus, and financial strains among some franchisees.
95 POLO RALPH LAUREN	2.05	1.93	+6	U.S.	Another record year for the preppy purveyor of American style that launched in 1967 as a line of flamboyant ties.
96 FEDEX	2.03	1.92	+6	U.S.	FedEx was riding high behind a successful expansion of its ground home-delivery service, stealing market share from leader United Parcel Service Inc.
97 BARBIE	1.87	1.94	-3	U.S.	The babe in pink reinvented herself as a DVD movie star, even taking a spin around Swan Lake. But she's slipping against fresh new competitors like Bratz.
98 WALL ST. JOURNAL	1.76	1.96	-10	U.S.	The downturn in advertising, especially for business publications, pummeled the Dow Jones flagship.
99 JOHNNIE WALKER	1.72	1.65	+4	Britain	Four bottles of this nearly 200-year-old blended scotch whiskey are consumed every minute, making it owner Diageo's most spirited brand.
100 JACK DANIELS	1.61	1.58	+2	U.S.	A global push and marketing campaign to appeal to women and younger drinkers means Jack Black ain't just for Good Old Boys anymore.

The brand valuations draw upon publicly available information, which has not been independently investigated by Interbrand. Valuations do not represent a guarantee of future performance of the brands or companies.
Data: Interbrand Corp., J.P. Morgan Chase & Co., Citigroup, Morgan Stanley, *BusinessWeek*

Creating and managing brand value

Interbrand

Founded in 1974, Interbrand serves the world with 34 offices in 22 countries. Working in close partnership with our clients we combine the rigorous strategy and analysis of brand consulting with world-class design and creativity.

We offer a range of services including research, strategy, naming and verbal identity, corporate identity, package design, retail design, internal brand communications, corporate reporting, digital branding tools, integrated marketing services, and brand valuation.

We enable our clients to achieve greater success by helping them to create and manage brand value.

Creating and managing brand value **Interbrand**

As seen in Business Week, August 9-16 2004

SOFTBANK SON HAS A NEW BROADBAND STRATEGY

JOHN KERRY HIS NEW PLAN FOR FOREIGN POLICY

AMERICAN EXPRESS LAUNCHING A CREDIT CARD WAR

The McGraw-Hill Companies

BusinessWeek

ASIAN EDITION / AUGUST 9-16, 2004

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THE BEST GLOBAL BRANDS

Our Annual Ranking of The Top **100**

SPECIAL DOUBLE ISSUE

Harley-Davidson is No. 41

BRAD TRENT

As seen in Business Week, August 9-16 2004

SPECIAL REPORT

CULT BRANDS

The *BusinessWeek*/Interbrand annual ranking of the world's most valuable brands shows the power of passionate consumers

CASEY NEISTAT, 23, IS A SELF-PROFESSED APPLE JUNKIE. Along with his brother, Van, he is building his filmmaking career with the company's iMac computers and editing software. He usually leaves his Manhattan apartment with a sleek iPod plugged into his ear. So last year, when the Neistat brothers discovered the digital music player's batteries were irreplaceable and lasted just 18 months, they made a film called *iPod's Dirty Secret* and launched a protest Web site. Apple Computer Inc. addressed the problem. Now Neistat insists that the protest was an act of love: "We made that film because we believe in the brand so much."

Such loyalty flies in the face of conventional marketing wisdom. A customer spurned, the logic goes, is a customer lost. But these days the relationship between brands and their customers has become much more complex. For one thing, consumers simply know more than they used to. The Internet opens up a wealth of information, allowing for instant price and quality comparisons. But consumers demand more from the brands they love than simple reliability; passionate consumers want their brands to become a form of self-expression. Increasingly, consumers are customizing products and services to achieve that—whether it's tailoring colors on a pair of sneakers from Nike Inc. or adding items to their personal to-watch list on eBay. Instead of arms-length customers, they're beginning to act like and feel like owners or members of a community. They no longer passively consume. Through the Internet, they can talk back and talk to one another. They can ignite a groundswell of positive buzz or spawn a revolt. As Peter Weedfald, senior vice-president for strategic marketing and new media at Samsung Electronics North America, puts it: "Consumers are empowered in a way that's almost frightening."

The World's 10 Most Valuable Brands

A newcomer, Toyota, breaks into the Top 10, while big-name consumer brands come under attack

RANK	BRAND	2004 BRAND VALUE (BILLIONS)
1	COCA-COLA	$67.39
2	MICROSOFT	61.37
3	IBM	53.79
4	GE	44.11
5	INTEL	33.50
6	DISNEY	27.11
7	McDONALD'S	25.00
8	NOKIA	24.04
9	TOYOTA	22.67
10	MARLBORO	22.13

Data: Interbrand Corp., J.P. Morgan Chase & Co., Citigroup, Morgan Stanley

As seen in Business Week, August 9-16 2004

ICONIC From Beijing to Boston, iPod users have formed a bond

QUENTIN SHIH/ASIA IMAGES

This seismic shift in clout from companies to their customers is creating opportunities, especially for younger brands that grew up with the Internet and have become adept at building user communities. Meanwhile, some traditional brands, such as Coca-Cola and Microsoft, are struggling to retain their mammoth leads in a market where consumers increasingly resist what they see as bland ubiquity and a surfeit of power.

There have always been cult brands, mostly smaller labels unknown to the masses. But these days, building cults or at least strong communities, is a widespread strategy. No wonder companies that are able to instill a sense of ownership in near-fanatical customers showed the biggest gains in our fourth annual ranking of the 100 most valuable global brands. The loyal, if sometimes nagging, band of true believers behind No. 43 Apple—combined with tremendous success of the iPod—helped the dollar value of the brand jump 23.7%, to $6.9 billion, over the past year. That was the biggest increase in this year's ranking, which is compiled in partnership with leading brand consultancy Interbrand Corp. A dollar value is calculated for each brand using a mix of publicly available data, projected profits, and variables like market leadership.

Apple was hardly alone in enlisting recruits. EBay makes its debut at No. 60. Fellow hot property Samsung Electronics, No. 21, jumped 15.7% in value to $12.6 billion—a move that Seoul-based global marketing chief Eric B. Kim attributes to "building communities around our brand." Along with honing a high-end image with its feature-packed cell phones and flat-panel TVs, it nurtures loyalty with events for users. Yahoo! and Amazon.com, Nos. 61 and 66, respectively, also made significant gains. But success isn't limited to the young. Cult icon Harley-Davidson, No. 41, climbed despite having been founded more than a century ago. While the value of those brands is a fraction of the top-ranked $67.4 billion Coca-Cola brand or No. 2 Microsoft, with $61.4 billion, those behemoths have lost brand value over the past year. And they, too, have started to recognize the need to nurture stronger ties with consumers. Witness moves by Microsoft to hold mini trade shows in airport lounges for consumers and the soda giant's creation of hip "Coke Red Lounges" for teens in suburban malls.

Group Think

THE GOAL: TO FOSTER A SENSE of shared experience and of belonging. Starbucks Chairman Howard D. Schultz balks at the notion that his brand, which ranks 98th in our survey and jumped 12% in value this year, is about selling various iterations of coffee. Says Schultz: "The product is the experience." His shops may sell latte, but what people really crave is the hip, relaxed ambiance, the music, even the baristas who remember the regulars' favorite concoctions. Sounds crazy? Not to student Amy Berkman. Approach her at her favorite New York City outlet and she lets forth a stream of opinions on everything from

As seen in Business Week, August 9-16 2004

ideal chair configurations in the store to the type of mustard they should use on their ham-and-cheese sandwiches. "Something more tangy and grainy would work better," she says, sipping on her daily chai latte. She cares because this is where she hangs out with her friends. Berkman doesn't like coffee; she likes the experience of being at Starbucks.

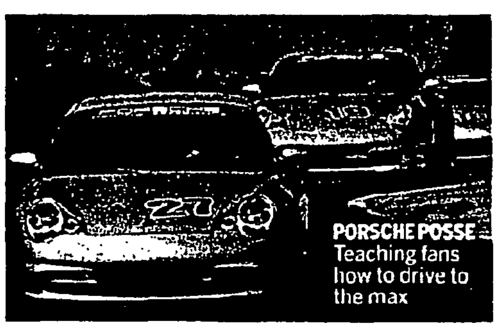
The brands that have managed to build cultlike followings have done so by being, well, cultlike, at least in some aspects. They are self-consciously different from rivals. They're bound by a set of clearly defined and rigorously enforced values. And they fulfill a range of needs for their members—er, customers. The fastest-growing ones often project an aura, an attractive group identity. Conjure up an image of an Armani customer or a Porsche driver and it will evoke a set of personality characteristics as much as it evokes a product preference. They also beget proselytizers—customers who will chat up the brands to their buddies, set up Web sites, attend events, and proudly identify themselves as adherents, according to strategist Douglas Atkin of ad agency Merkley & Partners, who recently wrote *The Culting of Brands*. Nobody has to pay them. They are owners as well as customers.

INTO IKEA Everyone loves the kids' section

Empowered Consumers

THE CLASSIC EXAMPLE of a cult brand is Harley-Davidson. The 101-year-old brand gained 4% in value this year to $7.1 billion. Sure, there are new models like the sleek V-Rod line and fresh features aimed at wooing women, but the real buzz comes from the 886,000 members of the company-sponsored Harley Owners Group. They're the ones who organize rides, training courses, social events, and charity fund-raisers. They pore through motorcycle magazines and wear the Harley-branded gear to feel more like rugged individualists and outlaws when they hit the road on weekends. A quarter of a million of them descended on Milwaukee last Labor Day to celebrate the brand's centennial. No wonder more than half of new Harley sales are to current customers who are trading up. The brand is self-reinforcing.

It doesn't take a cool category like motorcycles to yield a cult brand. Some are found in far more mundane sectors—like furniture retailing. In Shanghai, Wang Jian Shuo runs a Web blog that, among other things, delves into his likes and dislikes with No. 40 Ikea, the Swedish furniture chain that offers modestly priced, ready-to-assemble furniture with cute names. He writes about everything from the 12¢ ice cream cones in the store cafeterias to how, as a newly graduated student in 1999, he spent his first month's salary on a "Billy Bookcase." Notes Wang: "Ikea seems to know my life better than



PORSCHE POSSE Teaching fans how to drive to the max

Cultlike brands are self-consciously different from their competitors

any other furniture brand." Among those posting responses to his musings are a Malaysian fan who started his own Ikea forum and another who makes jokes about Swedish meatballs.

Such exchanges underline a key aspect of brand communities in the modern age: They evolve in ways that the head office often can't control. Newly empowered consumers can appropriate and manipulate the brand in whatever way they want. The Neistat brothers' anti-iPod Web site has generated 1.4 million hits from around the world. And it's not just brand fans who can make a difference—or inflict damage. Witness the success of *Super Size Me*, in which documentary filmmaker Morgan Spurlock chronicled his decline in health while eating meals at McDonald's for 30 days in a row. Although it denies any link, McDonald's Corp. recently did away with the Super Size meal option. They called it a menu simplification.

The key for brand builders is to give empowered consumers a great product and the tools to use it however they want. Jeffrey P. Bezos, chief executive of Amazon.com, whose brand value grew 22%, believes there is a distinct community built around his brand, even though it's now used by more than 30 million people

As seen in Business Week, August 9-16 2004

worldwide. For him, community is defined as "neighbors helping neighbors make purchase decisions." That means allowing negative customer reviews, even if it sabotages a possible sale. It meant halting spending on conventional advertising last year to funnel money into cutting prices and improving service in the belief that the community itself would spread the word. What Bezos does control is the range and quality of his site's offerings. "The thing that we did early on is that we made it very easy for people to find very obscure products," notes Bezos. "If you're not doing something that people will remark on, then it's going to be hard to generate word of mouth."

Some companies are using mass customization to bind their customers ever more tightly to their brands. The efforts extend beyond the individualized Web pages that characterize Web sites like Amazon.com and eBay. It means allowing customers to set up fan sites on the Web or personalize items. Some companies, like No. 18 Honda Motor and Nike, offer tools to help customers put their imprint on a product—such as choosing unique color combinations and messages for their sneakers. But relinquishing control has proved to be hard for some marketers. No. 6 Walt Disney and No. 82 AOL have famously chased down fans for unauthorized use of copyrighted material. As brand "futurist" Andrew Zolli argues: "When you get to the point where you're suing your customers over their use of your brand, it's time to change your business model."

Even brands that have largely grown through acquisitions and smart pricing understand the importance of building a distinct image and fan base. As Peter Stringham, group general manager of HSBC Holdings PLC bank in London notes: "Nobody needs a new anything anymore." Instead, what has allowed No. 33 HSBC to jump 15%, to $8.7 billion, this year is clear differentiation as "the world's local bank" with a flavor that varies by location. On Jan. 28, for example, it kicked off the rebranding of newly acquired Mexican bank GF Bital with a free live concert in Mexico City for 10,000 people by pop singer Luis Miguel. In New York, it grabbed attention by offering free taxi rides in a cab emblazoned with the bank's red and white logo to any passenger with an HSBC bank card.

In contrast, some old-line brands seem to be coasting on sheer size rather than an ability to forge a unique relationship with customers. Even brands that have enjoyed decades of success and have instant recognition with consumers can lose some sparkle. Over the past year heavyweights like Microsoft, Coca-Cola, and Walt Disney saw their brand values erode. Others, like Finnish mobile-phone giant Nokia Corp., No. 8, are struggling to regain momentum. "Nokia used to differentiate but I don't think people would know what to associate with it now," argues Jan Lindemann, Interbrand's global director of brand valuation. Nokia's head of global branding, Tapio Hedman, admits that "some young people may find Nokia too everyday, too middle of the road." But he disputes the notion that his brand could plummet 18% over 12 months, as it did this year in our ranking, arguing that brand equity takes years to win and lose. "Once you have it, it's a bit like insurance," says Hedman. "It's not likely to be eroded very fast unless you make one mistake after another."

That may be a dangerous point of view to take. Just ask Royal Philips Electronics' new chief marketing officer, Andrea Ragnetti, who blames the lack of buzz around the Dutch electronics giant, which dropped 2% in the rankings, to No. 65, on years of underinvesting in the brand. "It's seen as a dull, solid, reliable brand but nothing really special, nothing sparkling," says Ragnetti, who is currently trying to narrow the brand's target demographics and recast its message.

That doesn't mean big brands can't connect with customers. Even massive players like No. 4 General Electric Co., which saw its brand value gain 4%, to $44.1 billion, can adopt a fun, flirty style. The most popular section on the company's Web site is the "GE Pen," which allows users to doodle in a variety of colors and styles before e-mailing their handiwork to a friend. Since launching last year, it has received more than 43 million impressions. When the site went down for a few days to upgrade, the company was deluged with e-mails that asked where it had gone. Does it help the company sell more ovens or advertising on NBC? Probably not. But it certainly gives users a warmer feeling about GE. These days, anything that makes fans out of fickle consumers can be priceless in building a brand. ■

—By Diane Brady in New York, with Robert D. Hof in San Mateo, Calif., Andy Reinhardt in Paris, Moon Ihlwan in Seoul, Stanley Holmes in Seattle, Kerry Capell in London, and bureau reports

The Big Winners

It's the year of the iPod (Apple). Meanwhile, Net brands (Amazon, Yahoo) extend their reach, a Korean electronics juggernaut (Samsung) just gets stronger, and a London outfit (HSBC) stakes its claim as the world's local banker

RANK	BRAND	2004 BRAND VALUE (BILLIONS)	2003 BRAND VALUE (BILLIONS)	PERCENT CHANGE
43	APPLE	$6.87	$5.55	+24%
66	AMAZON.COM	4.16	3.40	+22%
61	YAHOO!	4.55	3.89	+17%
21	SAMSUNG	12.55	10.85	+16%
33	HSBC	8.67	7.56	+15%

Data: Interbrand Corp., J.P. Morgan Chase & Co., Citigroup, Morgan Stanley

The Big Losers

Technology and competition march onward, battering once-sterling brands in consumer photography (Kodak), video games (Nintendo), cell phones (Nokia), online service (AOL), and autos (Ford). Consumers ask: What's so special?

RANK	BRAND	2004 BRAND VALUE (BILLIONS)	2003 BRAND VALUE (BILLIONS)	PERCENT CHANGE
53	KODAK	$5.23	$7.83	-33%
46	NINTENDO	6.48	8.19	-21%
8	NOKIA	24.04	29.44	-18
82	AOL	3.25	3.96	-18
19	FORD	14.47	17.07	-15

Data: [illegible]

BusinessWeek online For an interview with Bezos and a Video View with Interbrand's Lindemann, go to businessweek.com/magazine/extra.htm

As seen in Business Week, August 9-16 2004

THE GLOBAL BRAND SCOREBOARD

The 100 Top Brands

Here's how we calculate the power in a name

LOTS OF INGREDIENTS go into ranking the world's most valuable brands. To even qualify for the list, each brand must have a value greater than $1 billion, derive about a third of its earnings outside its home country, and have publicly available marketing and financial data. One or more of those criteria eliminate such heavyweights as Visa, Wal-Mart, Mars, and CNN. We don't rank parent companies, which explains why Procter & Gamble doesn't show up. And airlines are not ranked because it's too hard to separate their brand's impact on sales from factors such as routes and schedules.

***BUSINESSWEEK* CHOSE** Interbrand Corp.'s methodology because it evaluates brands much the way analysts value other assets: on the basis of how much they're likely to earn in the future. Then the projected profits are discounted to a present value, based on the likelihood that those earnings will actually materialize.

THE FIRST STEP IS figuring out what percentage of a company's revenues can be credited to a brand. (The brand may be almost the entire company, as with McDonald's Corp., or just a portion, as it is for Marlboro.) Based on reports from analysts at J.P. Morgan Chase, Citigroup, and Morgan Stanley, Interbrand projects five years of earnings and sales for the brand. It then deducts operating costs, taxes, and a charge for the capital employed to arrive at the intangible earnings. The company strips out intangibles such as patents and customer convenience to assess what portion of those earnings is due to the brand.

FINALLY, THE BRAND'S strength is assessed to determine the risk profile of those earnings forecasts. Considerations include market leadership, stability, and global reach—its ability to cross both geographical and cultural borders. That generates a discount rate, which is applied to brand earnings to get a net present value. *BusinessWeek* and Interbrand believe this figure comes closest to representing a brand's true economic worth.

RANK 2004	RANK 2003		2004 BRAND VALUE $MILLIONS	2003 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
1	1	COCA-COLA	67,394	70,453	-4%	U.S.	Little innovation beyond its flagship brand and poor management has caught up with Coke as consumers' thirst for cola has diminished.
2	2	MICROSOFT	61,372	65,174	-6%	U.S.	Its logo pops up on 400 million computer screens worldwide. But virus plagues and rival Linux took some luster off Gates & Co.
3	3	IBM	53,791	51,767	4%	U.S.	A leader in defining e-business, with services making up more than half of Big Blue's sales.
4	4	GE	44,111	42,340	4%	U.S.	With acquisitions in areas from bioscience to bomb detection, it's easier to buy GE's new theme of "imagination at work."
5	5	INTEL	33,499	31,112	8%	U.S.	No longer just inside PCs, Intel is using its muscle to set the agenda for everything from wireless standards to the digital home.
6	7	DISNEY	27,113	28,036	-3%	U.S.	Long the gold seal in family entertainment, but newcomers like Nickelodeon and Pixar are siphoning off some of its brand equity.
7	8	McDONALD'S	25,001	24,699	1%	U.S.	Big Mac has pulled out of a two-year slump but still has to battle its reputation for supersizing the world's kids.
8	6	NOKIA	24,041	29,440	-18%	Finland	Tough times for the mobile-phone giant as its market share has slipped and younger buyers turn to rivals such as Samsung.
9	11	TOYOTA	22,673	20,784	9%	Japan	With rock-solid quality and the edge in hybrid cars, the Japanese auto maker is on track to overtake Ford in worldwide sales.
10	9	MARLBORO	22,128	22,183	0%	U.S.	The No. 1 name in cigarettes has cut prices and upped marketing to beat back the challenges of higher taxes and fewer smokers.
11	10	MERCEDES	21,331	21,371	0%	Germany	With wobbly profits and quality problems, the luxury car brand is struggling to retain premium status.
12	12	HEWLETT-PACKARD	20,978	19,860	6%	U.S.	Covering everything from digital cameras to service, the IT giant wants to dominate the middle ground between Dell and IBM.
13	13	CITIBANK	19,971	18,571	8%	U.S.	New CEO Charles Prince has spurred on global expansion and boosted the consumer credit division.
14	15	AMERICAN EXPRESS	17,683	16,833	5%	U.S.	A recent federal court ruling that allows banks to issue Amex cards should give the brand another boost.
15	16	GILLETTE	16,723	15,978	5%	U.S.	Despite the tougher competition from Schick, the King of Blades still reigns with new products like the battery-powered M3Power.

As seen in Business Week, August 9-16 2004

RANK 2004 / 2003			2004 BRAND VALUE $BILLIONS	2003 BRAND VALUE $BILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
16	17	CISCO	15.948	15.789	1%	U.S.	The networking behemoth used slick TV ads and key acquisitions like Linksys to extend its reach.
17	19	BMW	15.886	15.106	5%	Germany	The Bavarian auto maker is powering higher sales with a raft of new models from the sleek 6 Series sports coupe to the X3 baby SUV.
18	18	HONDA	14.874	15.625	-5%	Japan	Overtaken by Nissan at home and falling further behind rival Toyota in the U.S. market.
19	14	FORD	14.475	17.066	-15%	U.S.	Ford is trying to make quality "Job One" again after an embarrassing run of glitches, but leery consumers haven't yet regained trust.
20	20	SONY	12.759	13.153	-3%	Japan	It was late to the LCD TV boom, and the PS2 video game console is slipping. Worse, rival Samsung is in Sony's face.
21	25	SAMSUNG	12.553	10.846	16%	S. Korea	No longer known just for undercutting the prices of big Japanese brands, the Korean consumer-electronics dynamo is suddenly cool.
22	23	PEPSI	12.066	11.777	2%	U.S.	Targeted marketing and ads abroad with stars like soccer icon David Beckham have enabled the No. 2 cola maker to steal some of Coke's fizz.
23	21	NESCAFE	11.892	12.336	-4%	Switzerland	It's still the world's favorite instant coffee but even products like Ice Java struggle against hip upscale brands like Starbucks.
24	22	BUDWEISER	11.846	11.894	0%	U.S.	The growing global low-carb trend has left Bud flat. Plus, it's under attack from bulked-up and feisty rival Miller.
25	29	DELL	11.500	10.367	11%	U.S.	With its reputation for low prices and fast delivery, Dell continues to leave competitors in the dust.
26	27	MERRILL LYNCH	11.499	10.521	9%	U.S.	A painful overhaul is behind it. Now the retail brokerage is back in hiring and expansion mode.
27	26	MORGAN STANLEY	11.498	10.691	8%	U.S.	The investment bank's reputation is rising along with mergers and stock issuances, its specialty.
28	24	ORACLE	10.935	11.263	-3%	U.S.	The database-software business is up, but CEO Lawrence Ellison's fight to buy rival PeopleSoft makes Oracle look like a corporate raider.
29	28	PFIZER	10.635	10.455	2%	U.S.	The pharma industry's powerhouse, with 11 products each expected to top $1 billion in annual sales this year.
30	31	J.P. MORGAN	9.782	9.120	7%	U.S.	The marquee investment bank had a solid year, and now can extend its reach with its $58 billion acquisition of Bank One Corp.
31	33	NIKE	9.260	8.167	13%	U.S.	With allegations of sweatshop operations behind it and a growing soccer line, Nike rules the athletic market.
32	30	MERCK	8.811	9.407	-6%	U.S.	The drugmaker has tried to bolster its lineup with more partnerships, but patent expirations and research flops still pinch.
33	37	HSBC	8.671	7.565	15%	Britain	After snapping up Household International in 2003, the "world's local bank" is making inroads in the U.S. market.
34	35	SAP	8.323	7.714	8%	Germany	Its establishment image and sharp marketing have helped SAP thrive in a volatile software market.
35	39	CANON	8.055	7.192	12%	Japan	Hot digital cameras and printers boosted sales. Next up: an expanded line of sleek color copiers.
36	38	KELLOGG'S	8.029	7.438	8%	U.S.	Jumping on the low-carb bandwagon has kept Kellogg's cereal business crackling.
37	41	GOLDMAN SACHS	7.954	7.039	13%	U.S.	With record profits, it remains one of the most prestigious institutions on Wall Street.
38	36	GAP	7.873	7.688	2%	U.S.	The retail chain has revived its brand with fresh fashions and celebrity endorsements.
39	NEW	SIEMENS	7.470	New	New	Germany	The Munich conglomerate behind everything from phones to power plants is seeing a payoff from years of global image building.
40	43	IKEA	7.182	6.918	4%	Sweden	The Swedish home furnishing chain is now pushing cheap chic furnishings as far as Russia and Asia.
41	44	HARLEY-DAVIDSON	7.057	6.775	4%	U.S.	The motorcycle icon has lowered seat heights to woo women and trimmed prices, but production limits put a brake on growth.
42	40	HEINZ	7.026	7.097	-1%	U.S.	Despite wacky colors and cute ads, it's proving hard to boost value in foods like ketchup and beans.
43	50	APPLE	6.871	5.554	24%	U.S.	The iPod digital music player gave one of tech's coolest brands the consumer electronics hit of the year.
44	45	LOUIS VUITTON	6.602	6.708	-2%	France	It has a hot Murakami line and Jennifer Lopez in its ads, but is Vuitton getting over-exposed?

As seen in Business Week, August 9-16 2004

RANK 2004 / 2003			2004 BRAND VALUE $MILLIONS	2003 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
45	NEW	**UBS**	6,526	New	New	Switzerland	With a consolidated brand and its catchy "You and Us" campaign, the world's biggest asset manager is booming.
46	32	**NINTENDO**	6,479	8,190	-21%	Japan	It has an unrelenting focus on kids, but has Nintendo abandoned the gamers who have grown up?
47	46	**MTV**	6,456	6,278	3%	U.S.	The music network pumps cash for parent Viacom, and has an international reach that's the envy of U.S. media rivals
48	42	**VOLKSWAGEN**	6,410	6,938	-8%	Germany	Aging models and missteps make consumers write off the people's car as pricey and a bit dull.
49	47	**L'OREAL**	5,902	5,600	5%	France	Expansion in Asia and smart targeting of ethnic markets have the personal-care group looking prettier every day.
50	52	**ACCENTURE**	5,772	5,301	9%	U.S.	The tech services giant has its mojo back, with a contract to secure U.S. borders, and more consulting work.
51	48	**XEROX**	5,696	5,578	2%	U.S.	The copier maker is starting to convince customers that it can be a digital document one-stop-shop.
52	55	**WRIGLEY'S**	5,424	5,057	7%	U.S.	Sales are up as the gum maker looks to push popular brands into more mouths worldwide.
53	34	**KODAK**	5,231	7,826	-33%	U.S.	Removed from the Dow and only dominant in a film business that shrinks every year.
54	49	**KFC**	5,118	5,576	-8%	U.S.	Despite efforts to make the brand seem healthier, the world still focuses on the middle name in Kentucky Fried Chicken.
55	51	**PIZZA HUT**	5,050	5,312	-5%	U.S.	The low-carb craze crimped pizza sales, and the chain's tardiness in diversifying its menu didn't help
56	56	**COLGATE**	4,929	4,686	5%	U.S.	With a growing lead over Crest in markets from Russia to China, the toothpaste company is smiling.
57	54	**KLEENEX**	4,881	5,057	-3%	U.S.	The big name in tissues can't blow off fierce price-cutting by rivals or higher costs in pulp and paper.
58	57	**AVON**	4,849	4,631	5%	U.S.	The cosmetic company's door-to-door model is performing beautifully in foreign markets like Brazil and China.
59	53	**GUCCI**	4,715	5,100	-8%	Italy	Sales were slipping even before influential creative director Tom Ford said an April *arrivederci*.
60	NEW	**EBAY**	4,700	New	New	U.S.	With everything from vintage jewelry to new DVDs, it's where the world shops for bargains.
61	65	**YAHOO!**	4,545	3,895	17%	U.S.	The Internet portal has found riches in sponsored search but former partner Google is muscling into its turf.
62	60	**NESTLE**	4,529	4,460	2%	Switzerland	Chocolate is the key ingredient, but the Swiss giant is moving into nutritional supplements and fitness bars.
63	62	**DANONE**	4,488	4,237	6%	France	Strong sales of dairy products and bottled water keeps the French food company in good health.
64	61	**CHANEL**	4,416	4,315	2%	France	Successful couture and Nicole Kidman ads have kept this fashion house on people's lips, hips, and wrists.
65	59	**PHILIPS**	4,378	4,464	-2%	Netherlands	The Dutch electronics giant has scored some hits, but it's still struggling to fend off Asian rivals
66	74	**AMAZON.COM**	4,156	3,403	22%	U.S.	It dumped TV ads to cut prices, jump-starting sales and building its position as the Wal-Mart of the Web.
67	63	**KRAFT**	4,112	4,171	-1%	U.S.	There's new low-carbs packaging but critics accuse the food giant of producing products that make kids fat.
68	75	**CATERPILLAR**	3,801	3,363	13%	U.S.	The equipment manufacturer is plowing ahead as the industrial sector strengthens.
69	67	**ADIDAS**	3,740	3,679	2%	Germany	The German maker of athletic wear dominates in soccer, but is still trying to find its footing in the U.S
70	68	**ROLEX**	3,720	3,673	1%	Switzerland	For high-end consumers, the leading luxury watch maker's appeal is timeless.
71	76	**REUTERS**	3,691	3,300	12%	Britain	American CEO Tom Glocer's cost cuts and new products are helping the info giant turn the corner.
72	69	**BP**	3,662	3,582	2%	Britain	Now second only to ExxonMobil in size, BP is raking in cash thanks to high oil and gas prices.
73	66	**TIME**	3,651	3,784	-4%	U.S.	Softer advertising pulls down the brand even as its book division pumps out bestsellers.

As seen in Business Week, August 9-16 2004

THE GLOBAL BRAND SCOREBOARD

RANK 2004	2003		2004 BRAND VALUE $MILLIONS	2003 BRAND VALUE $MILLIONS	PERCENT CHANGE	COUNTRY OF OWNERSHIP	DESCRIPTION
74	NEW	PORSCHE	3,646	New	New	Germany	The high-end Cayenne SUV produced record profits and turbocharged the brand.
75	70	TIFFANY	3,638	3,540	3%	U.S.	The lure of its diamonds, pearls, and silver is strong but Japan is looking tarnished and U.S. store sales are down.
76	81	MOTOROLA	3,483	3,103	12%	U.S.	Motorola is relevant again, with its clam-shell phones gaining in Europe and in new markets like China.
77	79	PANASONIC	3,480	3,257	7%	Japan	It boasts some of the best technology in must-have items like recordable DVDs and plasma-screen TVs.
78	78	HERTZ	3,411	3,288	4%	U.S.	Healthy international markets help the king of car rental roar again, even amid rising gas prices.
79	73	HERMES	3,376	3,416	-1%	France	The maker of silk scarves and Kelly handbags hopes designer Jean Paul Gaultier can freshen its image.
80	71	DURACELL	3,362	3,438	-2%	U.S.	Relentless discounting and promotions continue to commoditize the world of batteries.
81	NEW	AUDI	3,288	New	New	Germany	The new A8 and strong global expansion have made Audi a profit engine. It's even thriving in China.
82	64	AOL	3,248	3,961	-18%	U.S.	Federal accounting inquiries and a messy merger have tarnished the AOL name as it fights to keep customers.
83	82	HENNESSY	3,084	2,996	3%	France	Parent LVMH is toasting the popularity of cognac with the world's young urbanites, especially among the hip-hop set.
84	83	SHELL	2,985	2,983	0%	Brit./Neth.	The energy giant is struggling to recuperate from a reserves downgrade and a boardroom bloodbath.
85	77	LEVI'S	2,979	3,298	-10%	U.S.	Even its iconic 501 jeans are discounted these days and brands like Diesel are finding legs with young shoppers.
86	85	SMIRNOFF	2,975	2,806	6%	Britain	The best-selling vodka builds on its popularity with Smirnoff Twist and "malternatives" such as Smirnoff Ice
87	86	JOHNSON & JOHNSON	2,952	2,706	9%	U.S.	Holding firm in a tough market, it had a hit with a drug-coated stent. But competition looms there, too.
88	NEW	ING	2,864	New	New	Netherlands	ING Direct and a forceful U.S. marketing push put the Dutch financial services firm on the map.
89	88	MOET & CHANDON	2,861	2,524	13%	France	Strong growth in Japan and the U.S. keeps the world's leading champagne brand bubbling along.
90	89	NISSAN	2,833	2,495	14%	Japan	Having pushed aside Honda in Japan, it's gaining North American share with Titan trucks and the Altima sedan.
91	NEW	CARTIER	2,749	New	New	France	The bejeweled panther has shed cheaper items and held tight to its luxury status through tough times.
92	NEW	ESTEE LAUDER	2,634	New	New	U.S	This fixture of the high-end cosmetics counter is now expanding in middle markets like retailer Kohl's.
93	NEW	ARMANI	2,613	New	New	Italy	Known for classy clothes, it's expanding into everything from home furnishings to hotels and restaurants.
94	84	BOEING	2,576	2,864	-10%	U.S.	It has lost commercial market share to rival Airbus, as execs try to erase the taint of a Pentagon hiring scandal.
95	87	PRADA	2,568	2,535	1%	Italy	Still the preserve of pretty stars but rapid expansion and debt could dilute some of Prada's exclusive cachet.
96	91	MOBIL	2,492	2,407	4%	U.S.	It got a boost from reformulated motor oil and its status as NASCAR's official lubricant.
97	92	NIVEA	2,409	2,221	8%	Germany	The mid-market skin-care line is now a leader in plumping up men's faces, too.
98	93	STARBUCKS	2,400	2,136	12%	U.S.	Global expansion, new products, and yet more variations on the humble cup of java boost the coffee hut's appeal.
99	90	HEINEKEN	2,380	2,431	-2%	Netherlands	Sales may be flat at Europe's largest brewery, but the 141-year-old Amsterdam brand remains the world's favorite premium brew.
100	95	POLO RL	2,147	2,048	5%	U.S	It has consolidated control of its clothing brand, pushing same-store sales up 11% in the last quarter of 2003.

The brand valuations draw upon publicly available information, which has not been independently investigated by Interbrand. Valuations do not represent a guarantee of future performance of the brands or companies. Data: Interbrand Corp., J.P. Morgan Chase & Co., Citigroup, Morgan Stanley, BusinessWeek

As seen in Business Week, August 9-16 2004

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Creating and managing brand value

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5 of 14 DOCUMENTS

Fortune

March 7, 2005

SECTION: U.S. EDITION; FEATURES/COVER STORIES/AMERICA'S MOST ADMIRED COMPANIES; Pg. 66

LENGTH: 1416 words

HEADLINE: America's Most Admired Companies;
Falling prices. Squeezed margins. Brutal competition. For this elite set of corporations, it's the perfect time to do business. Here's why the best prevail.

BYLINE: JERRY USEEM

BODY:

MURPHY HAD HIS LAW. HEISENBERG HAD A principle. And Warren Buffett has a saying: "When a management with a reputation for brilliance tackles a business with a reputation for bad economics, it is usually the reputation of the business that remains intact."

Far be it for us to challenge Mr. Buffett on this point, given his stature as the philosopher-king of American business and his penchant for good investment. But in examining this year's list of America's Most Admired Companies--which includes Buffett's Berkshire Hathaway at No. 7, by the way--we couldn't help but notice something: It's full of companies that flagrantly violate his dictum.

If your name is Southwest Airlines, for instance, you should be dying a slow death in the worst industry known to man. But instead, Southwest has just completed its 32nd consecutive year of profitability ... and it's one of only three airlines whose stock price actually rose last year ... and it looks perfectly comfy on that top ten above--just as it has for the past eight years.

If you're in the consumer products business, as Johnson & Johnson is, you're supposed to be sucking wind as store brands steal your shelf space and discounters take your lunch money. Yet there's J&J at No. 9. And there, just behind it, is Procter & Gamble.

Yes, if Buffett's Law were an actual law--and our Most Admired list were converted to a Most Wanted list--then post offices across America would be plastered with the boyish mug of Michael Dell. But then, his namesake company is thriving in an industry that may technically qualify as being in the poorest state in the Union. Its profits in this margin-squeezed business soared 15% in 2004, a feat that Dell makes look boringly routine. And now it's the first PC maker to hold the rank of America's Most Admired--since the original "PC" maker, IBM, logged off in 1986. (Check out the following story for some keen insights into how Dell continues to thrive.)

Is this a convergence of freak occurrences? Or do these uncommon companies have something in common?

You could employ all the usual adjectives and buzzwords and say that they're all smart and innovative. But there's something more remarkable going on here. What sets these companies apart--and connects them as a group--is their creative response to the phenomenon known as "commodity hell."

This next part should be read in a deep, eerie voice, preferably with an echo:

In commodity hell, everyone looks the same. Your products look the same, your margins look the same, and--wait a minute, where did those margins go? [Mad demonic laughter.] We hear they were spotted in Shanghai. [More mad laughter.]

"That is not a place I want to be," says a determined Jeff Immelt, CEO of General Electric, which earns bragging rights as the most globally admired franchise (and No. 2 on our American list). Immelt knows from experience. GE's light bulb business, for instance, went there around Edison's day and has yet to return. And Immelt doesn't plan on letting the company's other businesses go the same route. That's why he has been making big investments in frontier technologies--like nanometals, hydrogen power, and photovoltaics--where, to use Immelt's words, "very few can follow."

For P&G the road to commodity hell was paved with Prell shampoo--fading brands that could no longer command a premium on crowded superstore shelves. Its solution--cut 'em loose and circle the wagons around superbrands like Tide and Pampers (and soon, it hopes, Gillette razors)--has recharged its sway with consumers and challenged the encroachment of store labels.

So where is the encroacher-in-chief in all this? Where's Wal-Mart? Well, surprise, surprise--it's not trying to escape commodity hell so much as herd everyone else there with a pitchfork. It's the blue-vested boatman who is more than happy to give you a lift across the River Styx.

Not that Wal-Mart is alone in this strategy. Dell, too, loves the notion of commodity hell. In fact, it wants to turn its own product into a commodity. That would be crazy for a manufacturer of anything more complicated than a widget, perhaps. But Dell isn't really a manufacturer. In essence, it's a store--a store that assembles its wares at the last minute. The actual making of the products is left to suppliers.

Call it management judo: Don't resist the forces of commodification; use them to your advantage.

Gosh, this almost sounds easy. The problem is, once you've decided to rule commodity hell, you're in a permanent race to the bottom: You have to keep lowering your prices and somehow not go bust in the process. Your profit margins will often be slim; your margin for error will always be slimmer.

Gosh, this almost sounds impossible. And it nearly is--whether you're GE and P&G trying to gain pricing power or Wal-Mart and Dell trying to erase it. And that's why we admire all the corporations on this list. We admire what they do, to swipe a line from J.F.K., not because it is easy, but because it is hard.

Oh yeah, there's one more name on the list we forgot to mention--a company that sells a commodity. And we mean an actual commodity, whose futures are bought and sold at the New York Board of Trade. Its price has been dragging at historic lows--and yet you paid $ 3.55 for this morning's grande cappuccino.

Warren Buffett may still be the Oracle of Omaha. But if Starbucks proves anything, it's that industry isn't always destiny.

BOX STORY:

The Top Ten

1 Dell

2 General Electric

3 Starbucks

4 Wal-Mart Stores

5 Southwest Airlines

6 FedEx

7 Berkshire Hathaway

8 Microsoft

9 Johnson & Johnson

10 Procter & Gamble

BOX STORY:

Wal-Mart isn't trying to escape commodity hell so much as herd everyone else there with a pitchfork.

BOX STORY:

How We Did It

To conduct our survey, Hay Group polled a total of 15,000 respondents (executives, directors, and veteran securities analysts) around the world--10,000 in the U.S. and the rest in 21 other countries. We asked U.S. executives to rate the largest companies in their industry sectors in key categories. We've compiled their ratings in a complete industry list (see pullout). A large group of U.S. and non-American business leaders also judged 357 global corporations. Finally, we asked everyone to name the companies they most respect in any industry. The result: the two Top Ten lists we present here--America's and the world's Most Admired Companies.

BOX STORY:

Category Killers: The Eight Attributes of Reputation

Distilling a company's reputation isn't as easy as a quick thumbs up or down. There are too many variables (and constituents) to consider. So we narrowed the focus to eight specific areas of leadership, averaging our voters' scores to arrive at a final industry ranking (see the foldout section that follows for a complete list).

Innovation

Kinder Morgan Energy Partners 9.57

FedEx 8.82

Apple Computer 8.78

People management

Kinder Morgan Energy Partners 9.29

General Electric 8.84

American Express 8.67

Financial soundness

Kinder Morgan Energy Partners 9.43

Intel 9.40

Exxon Mobil 9.35

Quality of management

Kinder Morgan Energy Partners 9.86

Altria Group 9.14

Berkshire Hathaway 9.06

Use of corporate assets

Kinder Morgan Energy Partners 9.71

Berkshire Hathaway 8.94

Wal-Mart Stores 8.88

Social responsibility

United Parcel Service 8.95

CHS 8.86

Kinder Morgan Energy Partners 8.71

Long-term investment

Berkshire Hathaway 9.09

Kinder Morgan Energy Partners 8.86

CHS 8.71

Quality of products/services

Kinder Morgan Energy Partners 9.43

FedEx 8.94

American Express 8.88

BOX STORY:

Hay Group

Hay Group, which has conducted the research for the Most Admired Companies list since 1997, is a global human resources and organizational consulting firm with 78 offices in 43 countries. For more information about Hay Group's services, go to www.haygroup.com.

BOX STORY:

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Get detailed profiles on all of America's Most Admired Companies, including how they stack up against peers in innovation, talent, and more; sort the list by state; and find companies you most admire. Plus, see the complete list for both U.S. and global companies at www.fortune.com/ mostadmired.

To purchase corporate-reputation industry reports with attribute disclosure and five-year trend analysis, visit www.fortune. com/reputation, or call 212-522-6754.

GRAPHIC: COLOR PHOTO: PHOTOGRAPH BY GREG MILLER, TURBINE COWBOY, GE's 90-115B engine, the world's largest and most powerful, photographed in Cincinnati; COLOR PHOTO: MATTHEW MAHON, COLOR PHOTO: TOM SCHIERLITZ, COLOR PHOTO: LIVIA CORONA, COLOR PHOTO: GABOR EKECS

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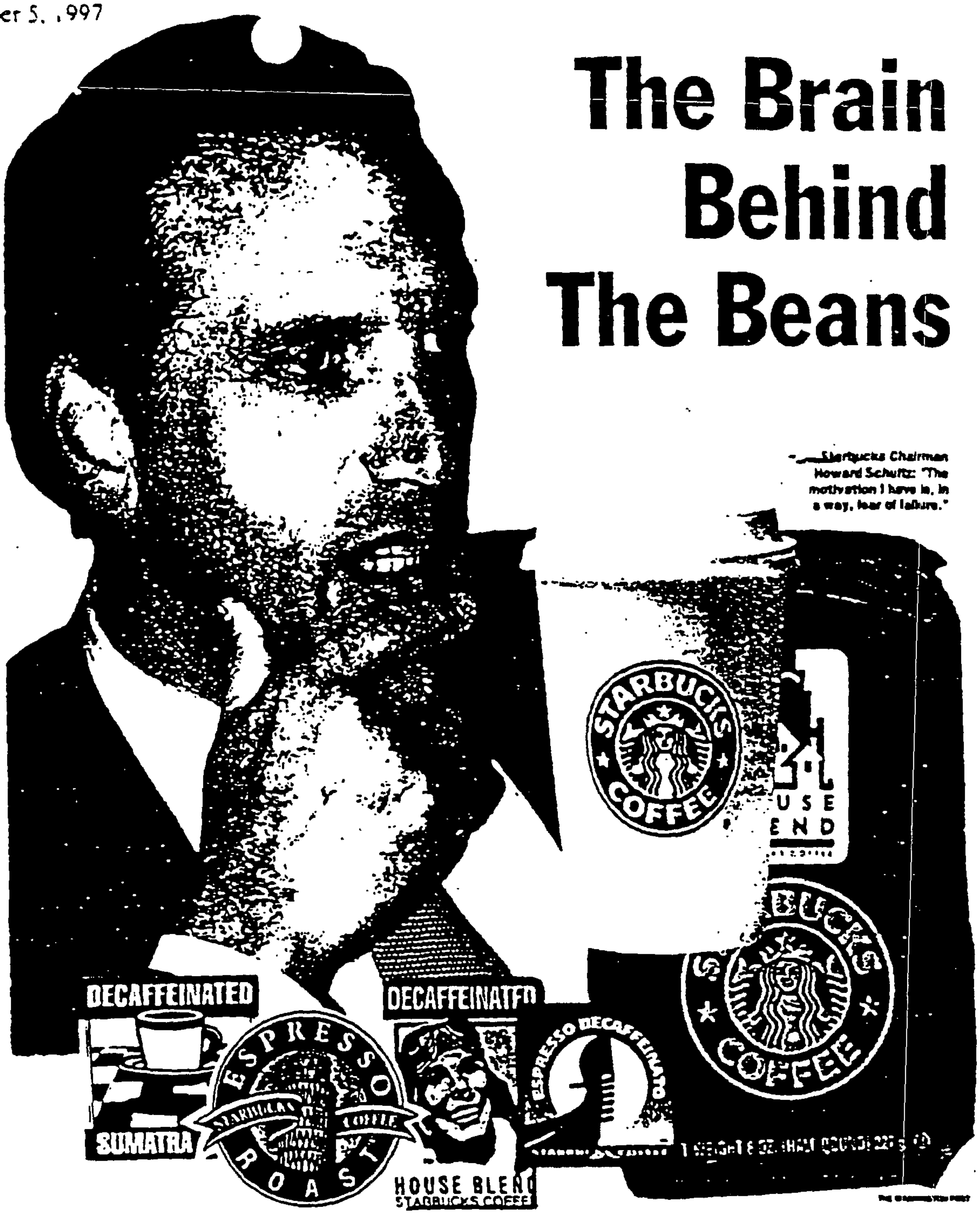
The Brain Behind The Beans



Starbucks Chairman Howard Schultz: "The motivation I have is, in a way, fear of failure."

Starbucks' Schultz Has Drawn Praise, Derision in Building His Coffeehouse Empire

By Margaret Webb Pressler
Washington Post Staff Writer

Howard Schultz, chairman of Starbucks Corp and a self-described "coffee purist," remembers that he didn't like the Frappuccino the first time he tasted it in 1994. It was, he thought, "kind of froufrou."

But it's a measure of Schultz's innovative, risk-taking company that the Frappuccino survived, despite the fact the boss didn't like it. The icy, blended coffee drink had been created by a Starbucks manager in California, who had experimented with the recipe and served it, without permission, to appreciative customers. It was the kind of risk that Schultz himself had taken on the road to building Starbucks, so it was not an effort he wanted to ignore.

The fact that the rest of his staff liked the drink, and told him so, was persuasive, too. So Schultz decided to test and refine the Frappuccino, and a year later it was rolled out to 550 Starbucks stores. That summer of 1995, it accounted for 11 percent of the chain's sales, and it has generated $100 million in revenue.

Schultz, 44, calls it the best mistake he didn't make and jokes that he now works for the woman who invented the Frappuccino. But the story is among his favorites, largely because it shows the entrepreneurial spirit that survives in a company that has grown, in a few hectic years, into a billion-dollar business.

"I do not want to build the kind of company that has bureaucracy in it," Schultz said. "I don't want to build processes and structure in a company where an idea like Frappuccino can't happen."

Starbucks' problem is that it has been so successful—and become so omnipresent on the American landscape—that it's the butt of jokes. Comedian Janeane Garofalo says Starbucks just opened in her living room. Jay Leno shows his audience a satellite picture of life on Mars: a Starbucks and a Gap.

And even as 5 million people a week gas up on its dark roast java, there may be an undercurrent of resentment brewing among people who view the latte-churning chain as an engine of the homogenization and strip malling of the landscape, as a cold machine bulldozing mom-and-pop coffee chains.

See STARBUCKS, H6, Col. 1

THE WASHINGTON POS (continued)
October 5, 1997

Schultz Faces Growth Challenges

STARBUCKS, From H1

But the man behind the beans isn't the rapacious executive Starbucks-haters may imagine. In fact, he's a charming, rags-to-riches guy who's really pretty hard to hate. And he takes criticism of his company very, very personally.

In a new autobiography, Schultz explains that he built Starbucks to be unlike the American businesses he knew as a kid growing up in Brooklyn. He wanted to give people the chance to drink great coffee. He also wanted to create a company that could offer health benefits and stock options, even to its part-time employees.

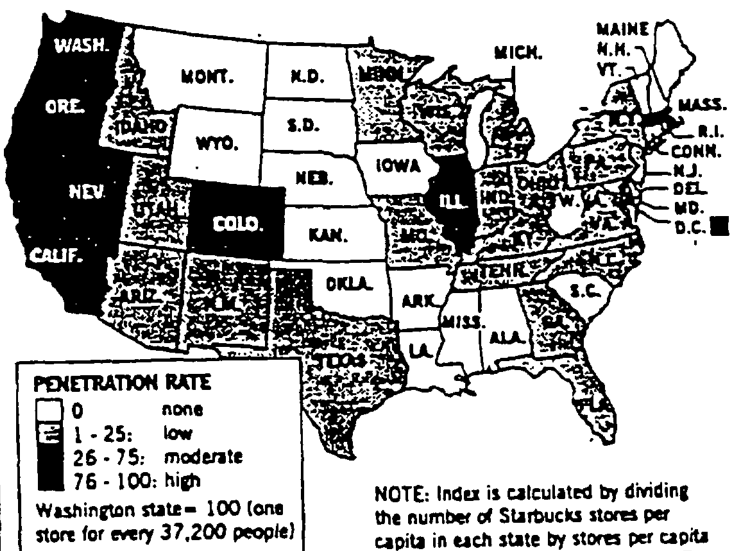
Schultz's challenge now is how to keep the Starbucks image from being tarnished by overexposure—and how to allow its original small-company spirit to thrive inside a big-company body, whose reach now extends to airplanes, ice cream, supermarkets and 1,350 coffee bars.

"When you're as successful as they have been, the temptation is essentially to start to conquer other horizons," said marketing consultant Jack Trout. The problem, he said, is that the bigger the company gets, the bigger the marketing department gets and the more MBA-types there will be parading through Schultz's office with "the idea of the month." Schultz, he warns, has to be able to throw them out.

"Size," Trout said, "is like a monster you've got to keep feeding."

STARBUCKS' PRESENCE

Although Starbucks stores seem ubiquitous in D.C. and Washington state, there is still some unexplored territory.



NOTE: Index is calculated by dividing the number of Starbucks stores per capita in each state by stores per capita in Washington state, as of April 1997.

SOURCE: Pacific Crest Securities

THE WASHINGTON POST

Broken Ankle, Broken Dreams

Starbucks never would have happened without Schultz. And it probably wouldn't have happened if Schultz's father hadn't broken his ankle when young Howie was just 7 years old.

The driver for a cloth diaper service, Schultz's father lost his job and his meager income with that injury. The wrenching aftermath, when his parents did not have enough money to feed the family, is seared into Schultz's memory.

As a child, Schultz was full of shame and anger about his circumstances, refusing, for example, to go back to summer camp when he learned it was a subsidized program for underprivileged kids. As a young man, he dreaded talking to the fathers of girls he dated, for fear they would ask him where he lived.

"The motivation I have is, in a way, fear of failure," he said. "I didn't want to be like that. I wanted to try to build the kind of company that would not leave people behind."

The best way not to be left behind, for a kid from the projects, was to be a good athlete. So Schultz played sports of all kinds—baseball, basketball, football—from morning till night, and his intense competitiveness helped him excel.

As the quarterback for his high school, Schultz was recruited to Northern Michigan University on a football scholarship. Though he never played football there, he became the first person in his family to earn a college degree.

After graduation, Schultz entered the Xerox Corp. training program, and his uncanny ability to connect with people made him a successful salesman. He went on to run the U.S. operations for a Swedish housewares company—selling, among other appliances, espresso machines.

That's how Schultz, newly married and living in Manhattan's Upper East Side, came to know Starbucks, a crunchy, new-age chain of four stores selling coffee beans and coffee-making products to an avid Seattle fan club.

Starbucks exerted a magnetic draw on Schultz's steely ambition, and he left New York in 1982 to work for the brash coffee company as director of Starbucks' retail operations and marketing. He wanted to push Starbucks the way he pushed himself. But he pushed a little too hard.

In 1984, Schultz had an insight that eventually changed the face of American retailing. While on a trip to Italy, he was struck by the profusion of coffee bars, and the way they served as neighborhood gathering places. Why couldn't the same thing happen in America, he wondered.

Schultz's desire to turn the company into a coffee bar business was not shared by Starbucks' owners. He left and started his own espresso bar chain, *Il Giornale*. Two years

MORE

THE WASHINGTON P((continued)
October 5, 1997

later, he had the money to buy out Starbucks, keeping its name, its beans and its people, but turning it into *his* concept.

"He's almost a caricature of an entrepreneur," said Warren Bennis, distinguished professor of business at the University of Southern California and an expert on leadership. When Schultz spoke to a conference on leadership in Los Angeles last week, he "had 500 executives on their feet applauding him," Bennis said. "And these are highly cynical people."

Courting Investors

The true test of Schultz's dream was raising the money to make it happen. By courting investors around Seattle during the late 1980s, he was able to open about 50 espresso bars. But to continue growing, he needed the help of investment banks.

Dan Levitan, then running the Los Angeles office of the investment bank Wertheim Schroder & Co., was cajoled into visiting Starbucks in 1991. He was persuaded to do so by a colleague who was marrying a woman from Portland, Ore., where he had gotten to know Starbucks.

Levitan said Starbucks "was a dream more than a company" at that point. And though he was touched by Schultz's devotion to giving all employees health care and stock options, it was "kind of a B-plus meeting," he said.

But as Levitan was leaving, Schultz looked him in the eye and said, "You know what's wrong with your business? There aren't enough *mensches* in your business," Schultz said, using a Yiddish word that people who are decent and honest.

"I looked at him, frankly, shocked," Levitan said. "How does he get so comfortable in the first meeting to say there aren't enough *mensches*? I would say after an hour and a half I'd never had that kind of interchange with a CEO."

Levitan began selling the Starbucks story, to anyone who would listen, from the Airfone on the plane back to Los Angeles. Few people "got it," Levitan said, but he invested personally in Starbucks—in Schultz.

In 1992, Levitan's firm became the co-underwriter of Starbucks' initial public offering, along with Alex. Brown & Sons Inc. of Baltimore. The stock Levitan first bought at about $2.25 a share is now worth about 20 times that.

Now an independent dealmaker, Levitan retains his interest in Starbucks and is an informal adviser to Schultz. He says that what has made the coffee venture so successful is that Schultz has surrounded himself with the brightest, most experienced executives he could find.

"Starbucks has become much bigger than he is, and to his credit, I think he's really happy about that," Levitan said.

Sharing Success

Schultz is a hero among his employees. And no wonder. Though many are part-timers, each employee gets a stock grant worth 14 percent of their salary at the end of every year. Because the stock plan vests over four years, the benefit is greatest for employees who stay for several years.

For a few of Starbucks' long-time employees, the stock plan has bought some serious lakefront real estate. But for most, it just helps with college tuition or the mortgage payments. The stock plan and other benefits have helped give Starbucks one of the lowest turnover rates of any retailer in the country, according to industry analysts.

And for Schultz, it makes him feel good. "A great part of the American dream is that . . . nobody should be left behind," he said. "That's the kind of company my father did not work for, and that's the kind of company we're building."

After D.C. Slayings, Mourning and a Crusade

Four months ago, Howard Schultz was awakened in the pre-dawn darkness by a phone call and told that three Starbucks workers had been brutally slain in Georgetown.

For a company chairman who prides himself on caring for his employees, the news was shattering. Schultz flew that morning from his vacation home in the Hamptons to Washington, where he spent the next days comforting the victims' families, attending their funerals and holding a memorial service for employees.

"None of us were prepared for this," he said.

Crisis management experts say Starbucks handled the tragedy just right—closing the Georgetown store, grieving with its employees, offering a reward. Local television stations showed the mother of a murdered McDonald's employee wondering in her grief why the fast-food chain hadn't responded to her loss the way Starbucks had.

Even Schultz's friends were struck by his reaction. "The most amazing thing about it," said financial adviser Dan Levitan, "is that he was really, really, deeply troubled for weeks by what happened in that Georgetown store."

Schultz is now pained by the fact that no one has been caught and held accountable for the killings. Though he treads lightly on the subject of the investigation—especially given recent criticisms of the Metropolitan Police Department's homicide detectives—Schultz clearly is not happy. The chain recently upped its reward from $50,000 to $100,000 and cooperated with "America's Most Wanted" for a recent episode on the crime show.

"I'm not satisfied with the result," Schultz said.

The store, meanwhile, will reopen before the end of the year, and its profits from now on will go to a foundation for the victims of violent crimes.

"I have promised the families that I will not rest until the people responsible for this are brought to justice," Schultz said. "I think it's an indictment on American society and random violence that something like this could happen in the heart of the nation's capital, on July Fourth weekend, at a place like Starbucks."

— Margaret Webb Pressler

MORE

THE WASHINGTON POST (concluded)
October 5, 1997

The desire to communicate this vision is one of the reasons Schultz has given every employee a copy of his book—aptly named "Pour Your Heart Into It." But with 26,000 employees now, intimacy and trust are not always possible.

One wrenching sign of of growth was the decision last year of employees at nine Starbucks stores in Vancouver to be represented by a union.

"It pained me to see that happen," said Schultz, "because I do not believe that Starbucks needs a third party involved with its people when we have demonstrated such a high degree of benevolence in making sure that our people are not left behind in sharing the success of the company."

"That is the greatest challenge the company has," he said. "Can something in America grow big and stay great? Most things have not."

Taking the Hard Knocks

These days Starbucks, which considers itself the consummate good guy, occasionally finds itself cast as the bad guy. Communities in Toronto, Portland and even Schultz's hometown of Brooklyn have demonstrated against the opening of new Starbucks stores that they say would put the local coffee merchant out of business. The late-night shows poke fun at the company's expansion and the audiences laugh.

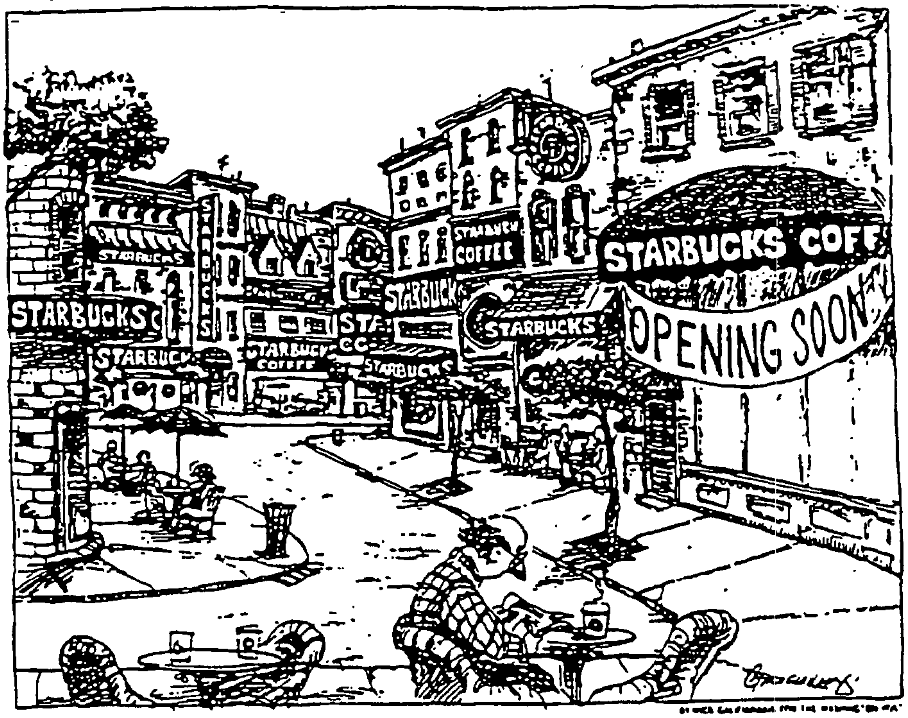
Schultz takes the knocks personally. "It is difficult when you try and do good work, try and build the kind of company that I think we're all proud of, and people for whatever reason don't like you. It's emotional," he said.

The company's sensitivity to criticism actually is helping it evolve, said John Rogers, an analyst with the Portland-based brokerage Jensen Securities. In real estate choices and store design, he said, "more and more I'm seeing them doing a very good job of blending into the neighborhood."

But what appeal does this new era of carefully managed growth hold for the entrepreneurial Schultz?

Schultz says he has graduated to the world stage. He is expanding his coffee-bar empire overseas; he is testing plans to sell Starbucks coffee in grocery stores around the United States, and he's spending millions of dollars on research and development to create new products and improve old ones.

"We're still in the infant stages of what we're going to be," Schultz insists. "Starbucks is going to be a global brand in the same genre as Coke and Disney and the great companies of our day."



IN PROFILE: HOWARD SCHULTZ


Howard Schultz in a Washington Starbucks

Title: Chairman, chief executive, Starbucks Corp.

Age: 44

Personal: Wife, Sheri; son, 11; daughter, 8.

Education: B.S. in communications, Northern Michigan University, 1975.

Career: Three years in sales and marketing for Xerox; vice president and general manager of Hammarplast U.S.A., a subsidiary of a Swedish housewares company. Joined Starbucks in 1982 as director of retail operations; started own coffee bar chain in 1985; bought Starbucks in 1987.

What he likes best about his job: Talking to Starbucks employees.

What he likes least: Talking to Wall Street.

Starbucks stock: Owns approximately two million shares, worth roughly $80 million, and another 1.5 million options on Starbucks shares.

Favorite coffee drink: Annual Christmas blend

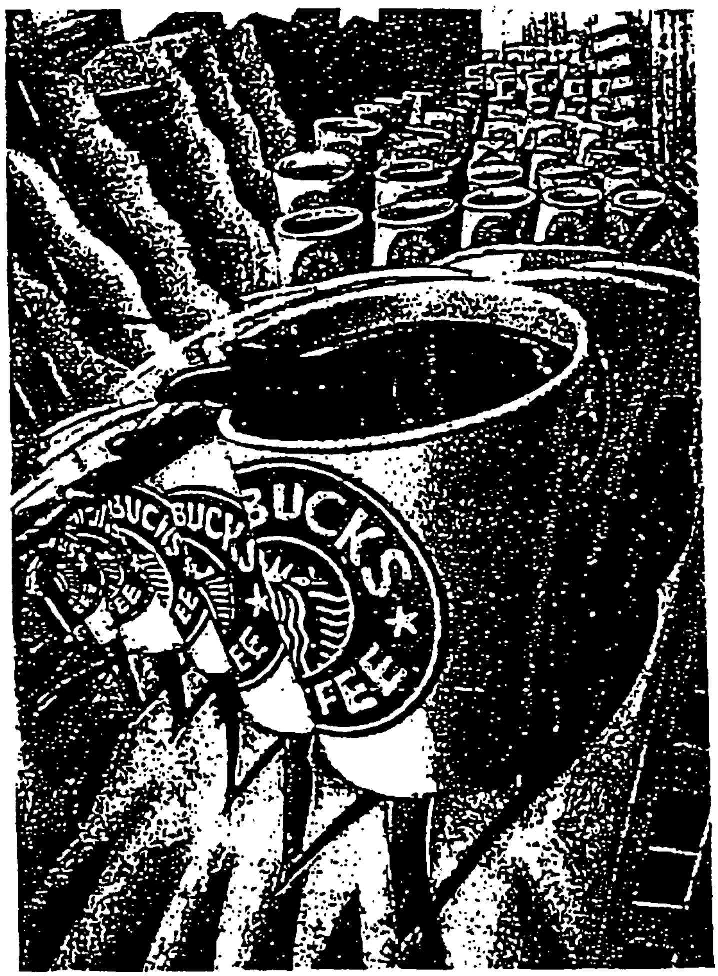
THE WASHINGTON POST

January 1998

The Starbucks Juggernaut

The green-and-white coffee stores are ubiquitous. But what is the master plan?

From a single store opened by three guys at Seattle's Pike Place Market in 1971, the Starbucks Coffee Company has grown into the McDonald's of coffee. There are, as you read this, nearly 1,400 stores in 28 states, the District of Columbia, three Canadian provinces, Singapore and Japan. The company planned to open 325 stores in fiscal 1997, and the goal of "2,000 by 2000" is starting to appear on coffee mugs throughout the company's headquarters.



"Starbucks is the most exciting growth story we follow," says Chris Vroom, an equity analyst for BT Alex. Brown. "We've watched it go from 20 stores to the almost 1,400 it has now. And there's still significant room for growth, especially internationally."

That's great news for java hounds who not so long ago languished in a coffee wasteland, a.k.a. the United States of America. If America's caffeine consciousness has now been raised considerably, it is in no small part thanks to Starbucks. The Specialty Coffee Association says there are more than 7,200 coffee outlets in the United States (if you include the 1,800 carts and 2,150 kiosks), up from 200 in 1989. "Much of that overall growth has to do with Starbucks," Vroom says. "They have done much of the heavy lifting involved in changing the way Americans think about coffee. They have created this atmosphere where people want good coffee. The whole industry has grown."

That influence on American tastes, as well as its lightning-quick expansion, led *Seattle Weekly* to posit that "Starbucks may join McDonald's and Holiday Inn in the pantheon of American businesses that changed the pattern of American life." Other publications say, more fancifully, that Starbucks has become the equivalent of a rural Irish pub, a place where people from a variety of walks of life come together and rub shoulders in a caffeine community.

But how long can Starbucks keep growing? After all, a quick review of the literature of brilliant starts turns up chocolate-chip cookies, frozen yogurt and premium ice cream as prime examples of overheated foodstuffs that didn't live up to their red-hot billings. What is the master plan?

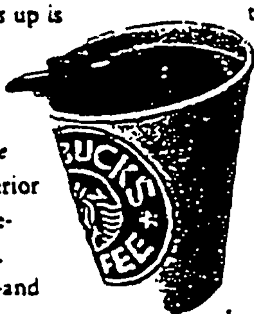
To begin to answer that, it's instructive to step back into the benighted past when Americans docilely accepted a coffee beverage that most Europeans would spit out in disgust, a brew so thin, weak and transparent that the French

MORE

among others, derisively referred to it as *pipi du chat* (a naturally occurring cat byproduct).

How could that be so? The rationing that world wars have induced has generally been no friend to coffee, an imported product susceptible to shortages and blockades. One of the most significant European wartime memories is of *Ersatzkaffee*, a faux coffee created, not happily, when coffee beans were not available. In Europe, though, as soon as trade in beans resumed significantly, coffee was brewed as it was remembered—and as it should be.

Not so in America. One of the most puzzling conundrums for those who fancy the kind of densely dark brew that Starbucks now serves up is how it was possible for coffee to be so routinely superior on one continent and *at the same moment* so routinely inferior on another among its presumed cultural offspring.



Blame a convenient—and appropriate—culprit: corporate America.

Coffee has followed the same sort of trajectory on the American palate as beer. As most people are now aware, American microbrews are a brilliant resurgence of local and personal individuality in beer making and a pointed rejection of the giant, standardized styles. In much the same fashion, there was a time when coffee was a very local product, roasted down the street, ground in the kitchen. The beans were then, usually, percolated—not the best way to make coffee (the brew is reheated) but a method that still yielded a strong cup of joe.

Then big companies got involved. The longer coffee beans are roasted, the darker they become, but they also begin to weigh less. To get the maximum weight—ergo maximum profit—from a given amount of beans, coffee companies encouraged consumers to use lightly roasted coffee, however awful the end product might be. They made the product convenient by marketing it in cans, with an "all-purpose grind." In addition, the directions on these cans recommended that consumers prepare their cups with amounts of coffee guaranteed to produce a bad brew. (Ironic, since encouraging consumers to use more, which would have produced a better brew, would have also enhanced consumption and demand.) As speed and convenience became more important than flavor, instant coffee became a hit. This is, after all, the country that created the term "fast food," and Americans have shown, certainly since World War II, an alarming propensity to sacrifice taste for convenience.

If America's caffeine consciousness has now been raised considerably, it is in no small part thanks to Starbucks.

Into this caffeinated quasi-desert stepped a former Xerox computer salesman turned coffee evangelist, Howard Schultz, who bought Starbucks from its founders for $3.8 million in 1987. Schultz had been converted to the world of good coffee while on a business trip to Italy. In his recently published book, *Pour Your Heart Into It: How Starbucks Built a Company One Cup at a Time* (Hyperion), he writes, "I discovered the ritual and romance of coffee bars in Italy. I saw how popular they were, and how vibrant. . . . It seemed they were on every street corner, and all were packed. . . . It was like an epiphany. It was so immediate and physical that I was shaking."

That defining moment partly explains the ubiquity of Starbucks. But there's another, simpler reason: profit, this time for retailers selling quality and atmosphere. A small but growing number of people are experiencing what [illegible]dia Roden calls "the Europeanization of American habits based on the sensual perception of taste." As a result, Americans not only want to know all about coffee—from plant to cup—but are also willing to pay a higher price for a great cup of coffee, just as they are for the refinements of a microbrewed beer. Equities analyst Vroom explains that Starbucks doesn't open two stores on the same block just for the collegial fun of it. It has to do with population density. "We estimate that some of their stores do $2 million a year in sales, with $1.3 million coming from coffee beverages," Vroom says. "The average purchase is $1.45, so that means that a single store is serving 900,000 drinks per year, or 2,500 drinks per day." With volume like that, it's little wonder a store opens across the street to relieve some of the pressure.

But Schultz can't really build one on every corner, can he? He can't have perfectly normal people dreaming of being baristas, can he? He can't turn the United States into Italy, can he—at least as far as coffee is concerned?

Probably not. Vroom predicts that Starbucks eventually will have 4,000 to 5,000 stores in the United States alone, a fraction of the more than 12,000 McDonald's outlets. Analysts and restaurant experts say that Starbucks will need to seriously upgrade its food if it hopes to continue its red-hot growth, and it will need to stay on top of its employees to maintain high levels of service. It will also need to address increasingly frequent opposition by community groups to the stores. Starbucks has met resistance from groups worried that a coffee bar—especially a corporate one—will change the nature of their little part of the world.

Despite the proliferation of coffee bars throughout the country, no other brand comes close to matching Starbucks' sheer size, organization, capitalization or quality. "There are some

MORE

SKY Magazine (concluded)
January 1998

companies, like Pasqua or Peet's in the [San Francisco] Bay area, that do a good job but are mainly regional operations," says Vroom. "Places like The Coffee Beanery are franchised, so the quality varies. Privately owned stores with good quality tend to be smaller and not nearly as well-run as a Starbucks. Starbucks is dominant in execution and has no national competition."

When Starbucks does face competition in an area it is moving into, the company has been known to make an offer that can't be refused. Starbucks absorbed The Coffee Connection, a small chain of high-quality stores in the Boston area, in 1994. Coffee Connection stores were turned into Starbucks stores, and the Connection's distinctive coffees (which were more lightly roasted than Starbucks' heavy "full-city roast"), while still offered in a few of the converted stores, are harder and harder to find. Currently, however, Starbucks is not in an acquisitive mode.

The communal aspect of the coffee bar is probably the company's most valuable asset. "When you go into a Starbucks, you see all kinds of people," says Linda DeAngelo, a professor of business administration at the University of Southern California. DeAngelo uses Starbucks' phenomenal growth as a model in her classes and believes that diversity is the key to the company's growth—and a potent sign of its robust prospects. "If all the customers were young people, I'd think that the coffee bar thing might just be a trend," she says. "But with old people and families in there, too, I think the future is very bright for them."

DeAngelo pauses before offering what is, in the end, Starbucks' raison d'être. "Besides," she says, "who wants to go back to drinking Yuban once you've had a Starbucks?"

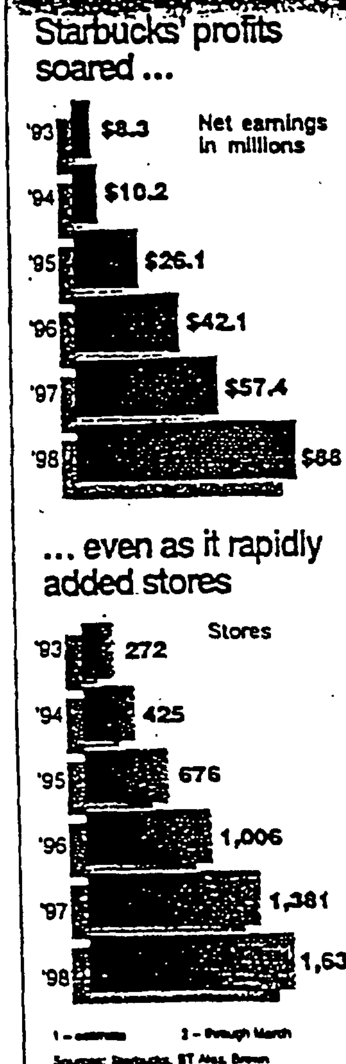
Writing this story will permit Sabrina Thompson to deduct her daily $3.25 for a double-short cappuccino, at least for a while.

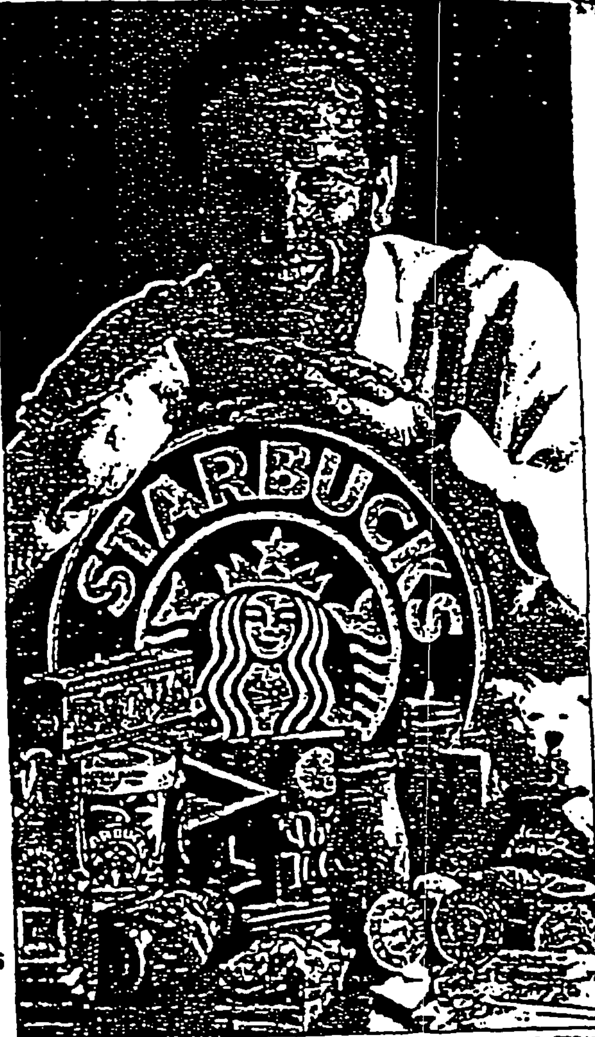
USA TODAY
April 30, 1998

Starbucks cultivates caffeine rush

By Bruce Horovitz
USA TODAY

Coffee giant branches out





CEO Schultz: 'We didn't set out to build a big brand.'

SEATTLE — Starbucks is treading on dangerous, new grounds.

The coffee king is pushing its brand far beyond the rim of the coffee cup. And well beyond U.S. borders.

The company said Wednesday it is moving into Europe by purchasing British-based Seattle Coffee for $81 million. Combined with Starbucks' entrance into Asia last year, the company soon may be opening as

COVER STORY

many stores overseas each year as it does domestically. That's more than 350 a year.

Starbucks may be synonymous with coffee, but it sells less than 5% of all coffee sold annually in the USA. And despite its aura of being as common as McDonald's, Starbucks stores are in just 29 states. Solution: Over the next two years, Starbucks plans to reach into almost every aisle of the nation's grocery stores.

After a year-long test in Chicago, the company this month began selling bagged coffee to 3,500 stores on the West Cost. It emerged as the nation's top seller of premium coffee ice cream its first year in grocery-store freezer sections. So it's no surprise that Starbucks is about to expand into the very cream of the ice cream category: chocolate and vanilla.

And later this summer, Starbucks is expected to announce plans to sell fresh fruit juice. The line still is in development.

Starbucks coffee shops are popping up everywhere — airports, bookstores, stadiums, movie theaters, grocery store kiosks, Laundromats and even Wells Fargo Bank branches. And in a recent joint venture with Earvin "Magic" Johnson, Starbucks has begun — for the first time — to open stores in the inner city.

The risk: dilution of the Starbucks name.

"Starbucks is a very powerful brand," says John Sicher, publisher of Beverage Digest. "But the landscape is littered with the carcasses of companies that have overextended powerful brand names."

But get ready. The real Starbucking of America has barely begun.

"We didn't set out to build a big brand," says chairman and CEO Howard Schultz. "But we now recognize that the power of the Starbucks name makes us capable of moving into other products and categories."

Starbucks the retailer is fast-evolving into Starbucks the megabrand. Coffee is still king at Starbucks. But coffee has percolated into a precursor of some decidedly noncoffee products. Inside the neighborhood Starbucks you now can find anything from $2 Starbucks breath mints (dubbed "After Coffee Mints") to $395 ceramic vases.

Nothing seems to be off-limits. The chain is experimenting with a line of jazz CDs and publishing ventures that tie in to Oprah Winfrey's book club. Its first national ad campaign kicks off next month — offering freebie samples of new coffee blends. And Starbucks is co-sponsoring one of this summer's biggest musical events, Lilith Fair 1998, featuring some of the nation's top fe-

Please see COVER STORY next page ▶

MORE

COVER STORY

Big markups drive Starbucks' growth

Continued from 1B

male singers.

Is Starbucks getting too big for its britches?

"They're becoming so large that consumers now associate Starbucks as corporate instead of quirky," says Tom Pirko, an industry consultant. "There's going to be a backlash."

Not if Schultz can help it. He's on a mission to grow the brand exponentially without turning its image into a McStarbucks.

Already, some small towns have waged heated campaigns to keep Starbucks out. The true test is whether the Starbucks name will eventually stand for quality or quantity.

Air Starbucks?

To oversee this delicate branding mission, Schultz has enlisted the help of Scott Bedbury, the former Nike marketing chief who many say was largely responsible for much of Nike's successful brand expansion in the late 1980s.

"This is what it felt like 10 years ago at Nike," says Bedbury, who heads Starbucks' new brand development department.

For 26 years, Starbucks has primarily represented a great cup of coffee to most consumers, Bedbury says. But in the future, when people think about Starbucks, "We want them to think about taking a break."

That, of course, can include a lot more than a cup o' joe.

"The best is yet to come," says Christopher Vroom, an analyst at BT Alex. Brown, who follows the company. "The next two years will be a watershed period for Starbucks."

The big driver behind Starbucks' growth: the tremendous profit it makes on each cup of coffee. The gross margin on its drip coffee is more than 70%, and the margins on its popular espresso drinks approach 90%, Vroom estimates. Nearly 55% of its beverage business is espresso drinks, he says.

"That kind of markup looks like rape and pillage to a lot of consumers," says consultant Pirko.

But Wall Street doesn't see it that way. Although Starbucks stock growth trailed the Standard and Poor's index of 500 big companies last year, Vroom projects earnings per share will grow 35% to 40% a year through the year 2000. Starbucks stock jumped 1$\frac{1}{16}$ Wednesday, to close at \$46$\frac{1}{2}$.

Vroom's optimistic outlook stems, in part, from plans to expand food service at Starbucks stores.

> "When Americans race from one voice-mail to one cell phone to one fax, there's a small oasis in their lives: their coffee break."
>
> — Howard Schultz, chairman and CEO, Starbucks

Starbucks salads

Soon, you'll be able to buy more than muffins and biscotti at many Starbucks. Real food — such as sandwiches and side salads — have sold well in tests in New York, Chicago and Seattle. That program will be expanded soon, Schultz says. But he won't consider hot foods — such as soups or pastas — because their cooking aromas could mask the smell of fresh-brewed coffee.

Starbucks retail stores are a handy testing ground for new products that eventually could sell at supermarkets. "Every store is a laboratory," Schultz says.

Its popular Frappuccino Coffee Drink originally was made to order at a Santa Monica, Calif., Starbucks store. The drink is now sold nationally — either made to order or in bottles that are distributed in a joint venture with Pepsi. And the company is testing Power Frappuccino — a vitamin-fortified version of the drink.

There are no plans for ice cream coolers any time soon at Starbucks, Schultz says. But its coffee ice cream joint venture at the supermarket with Dreyer's Grand Ice Cream has be[en w]ildly successful. Its first year, it was responsible for 50% growth in the entire premium coffee ice cream category. That's one reason its new Chocolate Chocolate Fudge ice cream is being rolled out next month. And vanilla ice cream later this year. At that point, there will be 10 ice creams under the Starbucks label.

Other products still under consideration: Starbucks-flavored coffee cake and even coffee-flavored chewing gum.

In fact, nearly 50 new products are now being tested in the company's product-development lab, says Senior Vice President David Olsen. This lab, deep in the bowels of the Starbucks Center headquarters, is off-limits to most Starbucks employees. But USA TODAY was granted the first-ever tour by any publication.

In the center of the lab sits a costly contraption developed specifically to test how to brew Starbucks quality coffee at jumbo jet altitudes. After this pressurized coffee brew tray was perfected in 1995, it was shared with United Airlines, which now serves Starbucks coffee.

Coffee flops

Not all new products have been hits for Starbucks. Mazagran, a carbonated coffee drink it tested with joint venture partner Pepsi, was a flop. But Schultz says he's interested in reintroducing an improved version of it "within three years."

And Red Hook Ale briefly brewed a beer with a hint of Starbucks coffee. But it's since been yanked.

"You can't expect we'll hit a home run every time out," Schultz says.

All this is a far cry from the first Starbucks store — named after the coffee-loving first mate in *Moby Dick*. The initial Starbucks opened in 1971, across from Seattle's famous Pike Market as a retailer of whole bean coffee. Consumers couldn't get a cup of coffee there. Just the beans to make it.

Ten years later, Schultz stumbled upon the store, and in 1987, he bought the company for about \$4 million. At the time, it had just six stores.

Today, there are 1,636 Starbucks stores in the USA, Asia and Europe.

The Starbucks empire may yet be in its infancy. But competitors take the chain very, very seriously.

Starbucks quietly made it known that its eyes were on Europe. But even before Starbucks opened its first store there, the British-based Seattle Coffee, which operates 56 Starbucks-like coffee shops in the London area, threw in the towel and sold to Starbucks on Wednesday.

"Better to work with Starbucks," says Scott Svenson, CEO of Seattle Coffee, "than to work against them."

King Bean

STARBUCKS CEO HOWARD SCHULTZ RUNS A $1 BILLION COMPANY THAT HAS A SUCCESSFUL MESSAGE FOR SMALL BUSINESS: CREATE VALUE AND ALWAYS FOCUS ON CUSTOMER SERVICE.

Starbucks Coffee Corp. chief executive Howard Schultz never thought the dream he started out with in his hip pocket would take him so far. In just ten years, this former on-the-road salesman for Xerox, who was raised in the Bayview Projects in Brooklyn, has grown a six-store Seattle coffee-bean retailer into a megachain of Italian-style coffee bars. Today the $1 billion Starbucks operates more than 1,500 stores from Boston to Dallas to Singapore. Schultz's 25,000 employees serve up savory brews—from creamy iced-coffee drinks like Frappuccinos to foamy concoctions like steamy caffè lattes—to about six million Americans each week who line up at Starbucks for a caffeine fix.

How did this rags-to-riches story begin? Schultz got his first break when a recruiter from North Michigan University came to one of his high school's football games, saw him make some swift moves as quarterback, and offered him a full scholarship. After graduating from college in 1975, he returned home to New York City and landed a job with Xerox in the sales-training program. After six months of making 50 cold calls a day, he developed elephant skin and a dogged determination. Four years later he landed a job as vice president of U.S. operations for Hammarplast, a Swedish housewares company.

But the turning point in his life came in 1981, when he noticed the strange buying patterns of a client called Starbucks Coffee, Tea, and Spice. The little Seattle retailer, named for the coffee-guzzling first mate in *Moby Dick*, was placing more orders than Macy's for a special kind of drip coffeemaker. Schultz was so intrigued that he made a pilgrimage West to learn more about the coffee company. There he was impressed with the

Howard Schultz: "If I did not take a risk, my moment would pass."

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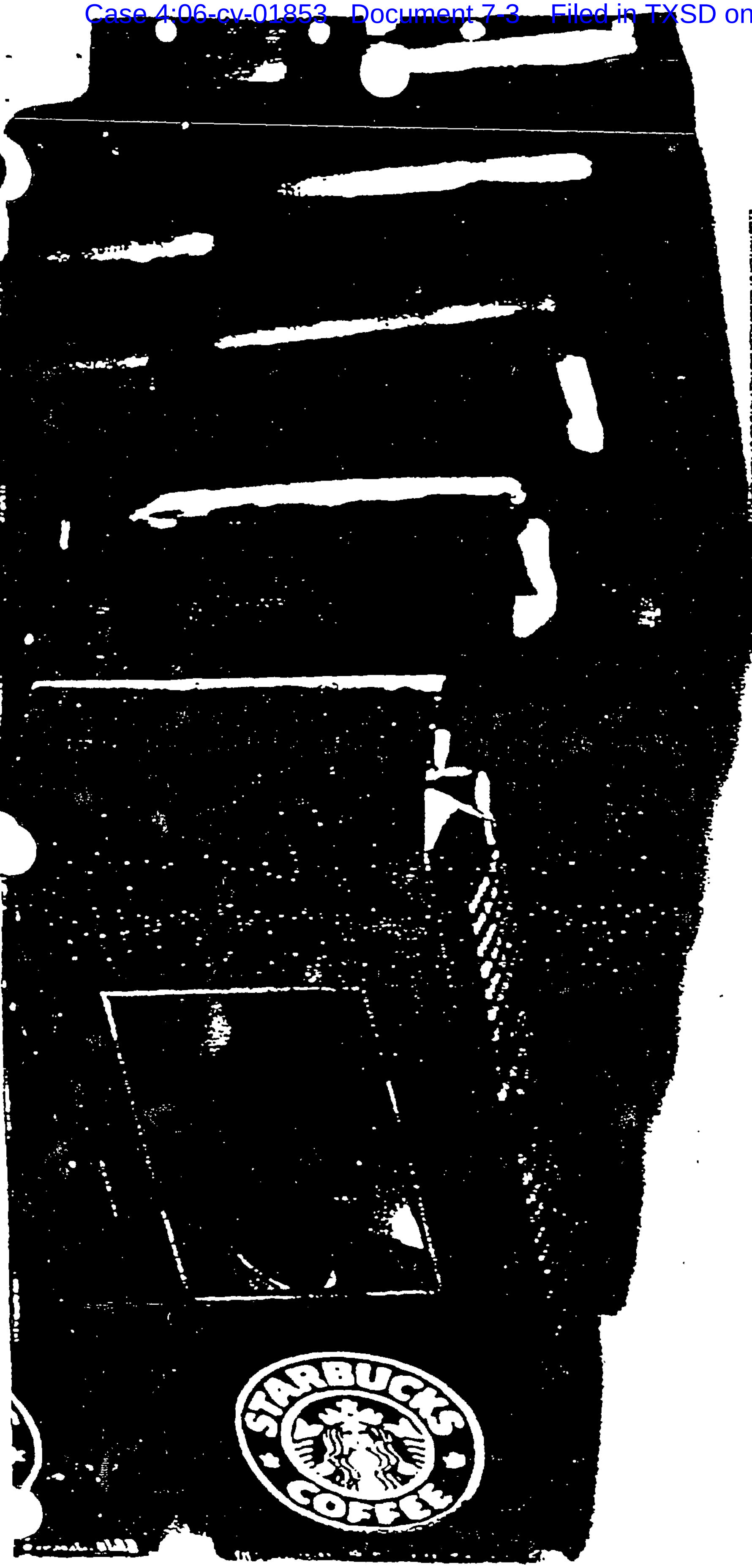


quality of the retailer's product, the character of its stores, and the following it had with loyal customers in its niche market. Within a year Schultz quit his job and persuaded Starbucks' partners to give him an equity share in the business. "It was *bashert*," he recalls, which means "destiny" in Yiddish.

During an interview with YOUR COMPANY senior editor Lori Ioannou in his office at Starbucks' corporate headquarters in Seattle, Schultz discussed his odyssey, which reveals how he grew his business into one of the country's most admired corporations and built a power brand on a shoestring budget. He also explained how important it is for entrepreneurs to pursue their dreams and take what he calls "leaps of faith" even when they are faced with cynicism from almost every quarter.

When did you get the idea to develop a chain of coffee bars on every street corner in America?

It happened in the spring of 1983. I had been at Starbucks for a year, and the company had sent me to Milan to attend an international housewares show. The morning after I arrived, I decided to walk to the show. During my stroll through the center of the city, I noticed espresso bars on almost every street corner. What struck me emotionally was the ritual and romance of each coffeehouse. The bartenders, called *baristas*, had a strong bond with customers. All kinds of people gathered and chatted at the bars, which served as extensions of the front porch in each neighborhood. Right then it struck me like a lightning rod: Why not bring the concept to America? Starbucks could be re-created to do just that. The vision was so overwhelming, I began shaking.

Why did you have a gut feeling that Americans would love espressos and cappuccinos as much as the Italians love them?

For the most part, Americans were not exposed to really good coffee. Most people were used to drinking coffee out of a can that was not fresh. That's why coffee consumption in America was

falling by 5% to 10% a year. I felt I could change all that if I introduced consumers to great-tasting coffee drinks Italians love, like espressos, caffè lattes, and cappuccinos—especially if such beverages were served in a romantic bistro setting like in Italy. That would just add more flavor to the experience.

Once you became obsessed with your vision, did you begin jotting down notes on the plane back to the States about how to transplant the concept?

As soon as the idea seized my soul, there wasn't a doubt in my mind that what I saw was the panacea for Starbucks. So then I raced home, not with a prepared business plan but with a passion in my heart to make this a reality. I didn't need to take down notes. What I needed to do was figure out a way to sell my two partners on my idea for Starbucks. I realized this would be a challenge, since my plan was bold and it meant reinventing the entire business.

Whom did you approach first with your new business idea?

I approached both of my partners, but neither became excited with my idea. The prospect of change did not appeal to them. The company was small and profitable, and they didn't want to lose control of the business with this thing. They felt that selling drinks wasn't consistent with what they envisioned the mission of a coffee store should be. They didn't want to be in the beverage business.

You must have been very frustrated after getting the cold shoulder. What did you do next?

I left Starbucks to start my own company. I decided that if I did not seize the opportunity and take a risk, my moment would pass and I would regret it forever. It was a tough decision, but I knew I had to take a leap of faith and believe in myself. It took courage. It was like deciding to jump off the side of a building with no net. Ironically, my former Starbucks partners became my first investors: they gave me $150,000 in seed money to start my enterprise, called Il Giornale. I began by flying back to Italy to research coffee bars, and I expected to come back with $1 million in financing. But all of the Italian companies I contacted weren't interested. So I came home and drafted a business plan on my kitchen table to attract investors through a private placement.

What made you think you could persuade angel investors to fork over millions of dollars to a new retail concept?

I was optimistic, and I truly believed in what I was doing. I think that helped me get through the whole humbling experience. If you want to know how underdogs feel, just try to raise money for a new venture. I went to anyone who I thought would write me a check. I knocked on everyone's door that I could find. Hundreds of investors turned me down. The rejection was painful. It took me one year, and I had to give up about 20% equity, but I raised $1.7 million from 23 individual investors, most of whom were prominent businessmen in Seattle. In the end their hunch paid off: Today they are million-

Extending the Brand

Starbucks is on a caffeine high. The company has rolled out a slew of new products and has entered into partnerships with businesses that sell them just about everywhere—even at 30,000 feet.

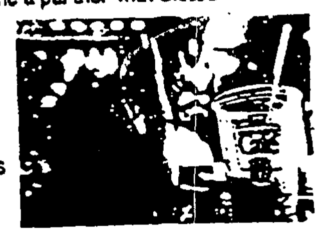
Gen Xer potable: There are some luxuries like bottled Frappuccino that consumers won't give up, not even at $1.50 a pop. This coolant, which is a lowfat, creamy, iced-coffee drink, is now being sold at Starbucks stores and supermarkets in the U.S. through a distribution agreement with Pepsi-Cola.

Bagged shoppers: Finally this spring, Starbucks coffee beans will be adorning supermarket shelves. The product will be rolled out in ten cities, including Denver and Los Angeles. It will be roasted just like the coffee sold in all Starbucks stores.

Frozen passion: Months after its introduction, Starbucks Ice Cream became the No. 1 coffee ice cream in the U.S. It is made through a joint venture with Dreyer's Grand Ice Cream.

The sound of music: Music is part of the Starbucks store experience. Starbucks often teams up with record companies to produce CDs to play during promotions. One of last year's favorites: *Africafe*, a collection of Afro-pop rhythms produced by Polygram Records.

Airborne sip code: As part of a global brand strategy, three years ago Starbucks became a partner with United Airlines to allow it to serve Starbucks coffee on flights.



Store within a store: In 1993, Barnes & Noble carved out a deal with Starbucks to open cafés within its bookstores. There are now 328 coffee bars that serve beverages and edibles to the merchant's customers.

aires. An investment of $100,000 in company stock back then is worth $10 million now.

So how did you eventually take over the Starbucks name?

After successfully opening two Il Giornale coffee bars in Seattle and one in Vancouver, I had heard that the Starbucks partners were selling the business—which included the six Seattle stores, a roasting plant, and the Starbucks name. Although my new company hadn't completed a full year of operations, I decided to jump on the chance to buy the Starbucks assets. The problem was, I had to go out again and raise $3.8 million to finance the deal. So I went back to my original investors. I did it in three months. By August 1987 Starbucks was mine, and I had the big a large and enduring company without a good foundation.

How did you jump-start the company's national expansion?

The key was getting capital and strategic-planning advice from venture capitalists who already had a successful track record building brands and large companies. I sought them out because I knew I needed a lot of financing and advice. I believe that every entrepreneur growing a business needs an outsider to give him or her perspective. They helped me transform Starbucks from a private company to a professionally managed public corporation. By the end of 1992 we had 165 stores in California, Colorado, Illinois, Oregon, and Washington, and our stock was traded on Nasdaq.

You've built a national brand at warp speed with hardly any advertising. Tell us how you pulled it off.

Since I bought the business, we've spent less than $10 million on advertising. Not because I didn't believe in it, but because I couldn't afford it. Instead we concentrated on creating value with the product and on customer service. Our store managers and workers have been the best ambassadors for the coffee and the brand. They make personal attachments with customers, who have spread the word ~~about~~ the Starbucks experience to family and friends. Our success proves you can build a national brand without 30-second sound bites.

Now that Starbucks is a huge public company, do you miss the thrill of running a small business?

"EVERY ENTREPRENEUR HAS TO TAKE A LEAP OF FAITH AND PURSUE HIS OR HER DREAM. I'M LIVING PROOF IT CAN BE DONE."

dream. It was hard, but I retired my company's name and decided to stick with the more established Starbucks name.

What were the biggest challenges you encountered when you took over?

When I took over Starbucks, it began to lose a ton of money. In 1987 we lost $330,000. The next year losses more than doubled. The third year we lost $1.2 million. That's because I decided to invest in an infrastructure for the company ahead of its growth curve. I hired experienced executives who had already built and managed retail companies and shared my values. I invested in a world-class roasting facility. And I bought a computer-information system sophisticated enough to keep track of sales in hundreds of stores. In addition, I began to offer health insurance and stock options to all of the staff—both part-timers and full-timers. That's because I knew my employees were the company's most valuable asset.

All of this took money. The losses made my investors and workers nervous. What I had to do was convince them that my novel idea was the right thing to do. I explained you can't build

What is the centerpiece of your retail formula?

That's simple: Exceed the expectations of our consumers by offering the highest-quality product and customer service. History has proved that our customers are loyal because we follow these principles. To maintain tight quality controls on the product and its distribution, I decided not to franchise stores—that's important, since store sales account for 87% of annual revenues.

Is that how you transformed a common cup of coffee into a coveted gourmet product?

From the beginning I concentrated our efforts on the coffee itself. I wanted to sell deeply roasted aromatic blends. The goal was to add value to a commodity typically purchased on supermarket aisles. At our stores our *baristas* introduce customers to the fine coffees of the world the way wine stewards bring forward the world's fine wines. They explain the different flavors and characteristics of coffees such as Ethiopia Sidamo to shoppers. Eventually patrons become coffee connoisseurs, and they keep coming back for another cup.

For me, the thrill has remained constant—it has just changed as the size and scope of my business has changed. Today I'm more excited than ever before. I like my hand. I feel the company is in a good position now to capitalize on the brand and keep growing.

What is the greatest responsibility an entrepreneur has when he builds a new business?

To create value for two constituencies: his employees and his shareholders. I learned from my father's personal experience that it's important to make sure your workers share in the success of your business and are not left behind. My dad was a blue-collar worker who never had health insurance or workers' compensation. When I was 7 years old he got sick, and the family had no income. Eventually he became a beaten man.

That left an impression on me, and I vowed back then that if ever I could make a difference, I would. By providing benefits even to part-timers, I've created a culture of passion and devotion in the organization—that's Starbucks' No. 1 competitive advantage. Now the secret is out of the bag.

Growing Company

With a special blend of employee benefits and a work/life program, one company has elevated a routine cuppa-joe to a supreme business entity.

How Starbucks Impassions Workers to Drive Growth

By Naomi Weiss

ou can't help but appreciate a company that routinely begins meetings with a coffee tasting. Or a corporate work setting where traditional conference rooms are replaced by parks resembling contemporary Euro-style cafes, where associates pour themselves a double tall latte, easy on the foam, and sit on a cozy couch alongside their "partners" and colleagues.

Welcome to the Starbucks Support Center, Starbucks Coffee Co.'s headquarters in Seattle. There's an energy here—not induced by a caffeine rush—but from associates drinking up a robust blend of teamwork, sense of mission and challenge. As one of *Fortune* magazine's 1997 "100 Best Companies to Work For in America," not to mention one of the world's fastest growing purveyors of indulgence, Starbucks has been giving its employees a daily lift since 1971.

Woven into the company's Mission Statement is the objective to "Provide a great work environment and treat each other with respect and dignity." But it takes more than company declarations to motivate and inspire people. So how does a young, developing company on an aggressive growth track motivate more than 27,000 people and inspire balance and camaraderie?

The answer is what Starbucks refers to as "a special blend of employee benefits" and a work/life program that focuses on the physical, mental, emotional and creative aspects of each person. This dynamic company developed an innovative work/life program to brew a committed coffee culture—and a passionate partnership.

Everywhere you look, there's Starbucks. Since Starbucks arrived on the scene, coffee isn't just a morning ritual. The ubiquitous Starbucks Coffee Co. brew has defined a fast-spreading trend from North America to Asia and beyond. Starbucks has met its goal of becoming a $1 billion company by the turn of the century. Its stock is up more than 800 percent since going public in 1992. And there's no question the company is one of the more phenomenal success stories.

Indeed, the Starbucks philosophy and the loyalty of its people have built a company with more than 1,700 stores worldwide, including a recent unveiling in the United Kingdom. The Starbucks blend can be found in restaurants, hotels, offices and airlines. The company also operates a mail-order business worldwide. Its retail sales exceeded $966 million in the 1997 fiscal year.

In little more than a decade, Starbucks elevated a routine "cuppa-joe" to its current supreme status. It operates in nearly every major U.S. metropolitan area, serving more than 5 million coffee lovers each week. Starbucks opens virtually a store a day. Turn on the television and witness "Frazier," "Seinfeld" and medics

on "ER" sipping Starbucks in the course of their prime-time adventures.

A global player, the company plans to continue expanding at 35 to 40 percent in coming years—an achievement possible only with committed, stake-holding associates. But Starbucks isn't just about a great cup of coffee. It's about people—and a humanistic approach to doing business that produces bottom-line results.

Ask Joan Moffat, the Starbucks manager of partner relations and work/life. A member of the HR team, she's responsible for the company's work/life program, which includes on-site fitness services, referral and educational support for child-care and elder-care issues, an Info-line for convenient information and the "Partner Connection"—a program that links employees with shared interests and hobbies.

Moffat, who worked in part with a benefits management organization, Portland-based Working Solutions Inc., says the investment pays for itself, and that many of the programs cost very little to implement. Starbucks has comparatively low health-care costs, reduced absenteeism and one of the strongest retention rates in the industry. "Our turnover rate is 60 percent, which is excellent as compared to the restaurant and retail industry," says Moffat. Moreover, employees reap the benefits of the company's ongoing success.

A shot of equity in every cup. "Seize the day" is a perfect motto for Starbucks. The company empowers its employees—or *partners* as they're regarded—to do just that. Starbucks is committed to providing an atmosphere that breeds respect and values the contribution people make each day, regardless of who they are or where they are within the company. All partners who work a minimum 20 hours a week receive full medical and dental coverage, vacation days and stock options as part of Starbucks *BEAN STOCK* program. The awarding of stock options to every level of the organization was unprecedented in the service industry a few years ago.

Starbucks Coffee Co. provides even part-time employees with health coverage, dental and vision plans, disability and life insurance. And those are just a few of the perks.

In addition to offering their "partners" many awards and benefits programs, Starbucks motivates its employees by emphasizing the importance of communication, and listening to their needs.

"We established *BEAN STOCK* in 1991 as a way of investing in our partners and creating ownership across the company," explains Bradley Honeycutt, vice president of human resource services. "It's been a key to retaining good people and building loyalty. Naturally, the level of our customer service is favorably impacted, as a result," she adds.

For those involved early on, the rewards have been especially generous as the company has grown and the price of Starbucks stock jumped from $17 to $46. In the process, the term "partner" was introduced throughout the company.

Just as with the *BEAN STOCK* program, all employees who work 20 hours or more a week are eligible for a universal benefits program. It's not just reserved for the corporate or managerial level. Eligible partners can choose health coverage from two managed care plans or a catastrophic plan. They also can select between two dental plans and a vision plan. Because of the young, healthy workforce, Starbucks has low health benefit costs. According to Annette King, HR benefits manager, the company's health-care costs are approximately 20 percent lower than the national average.

The company also provides disability and life insurance, a discounted stock-purchase plan and a retirement savings plan with company matching contributions. The benefits provide a powerful incentive to stay with the company, particularly among part-timers, thus reducing Starbucks' recruiting and training costs. "We have historically had low turnover, most of which can be attributed to the culture and a sense of community," says Moffat.

As anyone in the service industry realizes, finding and keeping good people is more difficult than ever before—and more important. Much of the company's ambiance—what makes its coffee experience particularly special—is its enthusiastic staff. Starbucks has discovered that when partners are actively involved in the company, the customer benefits and the bottom line grows.

That's why the statement "Bring ideas to the table" has real meaning at Starbucks. For example, the idea of a cold, coffee blended beverage, such as a Frappuccino® blended drink, was the collective brainchild of a few partners. And when one of the store managers began experimenting with customized in-store music tapes, the idea evolved into Starbucks-branded CDs, explains Moffat. That sense of contribution has translated into retention.

Some "baristas," or espresso drink makers, have been with Starbucks seven

PHOTOS STARBUCKS

AT A GLANCE

ORGANIZATION
Starbucks Coffee Company

INDUSTRY
Service

EMPLOYEES
[illegible]

HR EMPLOYEES
[illegible]

CHALLENGE
[illegible]

SOLUTION
[illegible]

RESULTS
[illegible] Employees value the benefits and work/life perks that come with the job.

or more years, which is particularly unusual for part-timers whose ranks annually turn over 300 percent at more conventional restaurants.

HR's challenge into the next millennium. Like many other U.S. companies, Starbucks is expanding in an era of corporate downsizing and economic belt-tightening. Its challenge is to meet customer expectations, while not diluting the company's culture and the contribution of every person.

Human resources' challenge is to ensure that the company's partner-based values survive its ambitious expansion into the new millennium. Therefore, HR takes stock in being a democratic operation, inviting ideas and solutions, and sharing in the rewards. To nurture open communications and innovative thinking, several Partner Relations mechanisms exist:

- *Mission Review* is a forum that encourages partners to tell the company how they're feeling and ask any questions. "Promote a very open environment ... here's what you've told us and here's what we've done," says Moffat. "We provide supportive action out of their comments." Partners always receive a response to their inquiries within two weeks. The goal of such openness: a feeling of internal respect.
- *Open Forums* are regularly held to examine performance, recognize achievements, plus look at the future. It's also another opportunity for partners to freely question upper management.
- The *Warm Regards* recognition program was developed to spotlight outstanding achievement that embodies the guiding principles, mission and goals of Starbucks. Specific awards include "The MUG (Moves of Uncommon Greatness) Award," "BRAVO!," which recognizes partner achievements and also "The Spirit of Starbucks," which honors passion and action.

We have historically had low turnover, most of which can be attributed to the culture and sense of community.

Joan Moffat, Manager of Partner Relations and Work/Life

None of these initiatives, of course, could gain hold without support from the top. Heading the java empire since 1987 is chairman and CEO Howard Schultz. What Wall Street and stockholders view simply as business acumen, Schultz sees as building a solid business with heart and soul. "We're profitable because of the value system of our company," says Schultz. "American companies have failed to realize that there's tremendous value in inspiring people to share a common purpose of self-esteem, self-respect and appreciation," he says.

He draws on his own personal experiences growing up in a rough, blue-collar neighborhood of Brooklyn, New York. The title of Schultz's best-selling book about the company, *Pour Your Heart Into It*, is no accident. It's an article of faith at Starbucks: How people are treated motivates a unified and committed operation.

Work/life benefits are part of the blend. Providing balance only makes sense to Schultz. To do so, the company must constantly evaluate employees' needs and wants by using opinion surveys and maintaining an open ear to partners. Such diligence is an intrinsic part of the culture Starbucks seeks to create.

Three years ago, human resources began examining how it could become more attuned to its partners. For instance, some employees who started with the company when they were in college are now buying homes and managing the realities of child-care and elder-care issues. Starbucks has responded by providing flexible work schedules as part of the work/life program. "Our environment lends itself to meet multiple life demands. By virtue of our strong sales and accelerated growth, flex schedules have not hurt productivity in the least,"

says Moffat. "Flexibility is particularly inherent in our stores because of our extended hours of operation and the diversity of our workforce—from students to parents—who need to work alternative hours."

HR also has engaged Working Solutions to offer a range of integrated benefit services that address the modern climate and culture of corporations—referred to as "non-traditional" benefits, or emerging needs. Working Solutions has trained life-event specialists who can help solve issues that require health, social, educational and counseling resources. In addition, Working Solutions offers online employee support anywhere in the world, 24-hours a day.

Recent studies have shown that 60 percent of American workers have child- or elder-care responsibilities. Starbucks recognized—as many other companies have—that partners less encumbered by personal stress and obligations are more innovative and productive. Working Solutions helped Starbucks implement several programs that specifically address the life stages and personal needs of its workforce. "Working Solutions' style of caring and support complements our work/life program, and helps ensure the quality our partners deserve," says Moffat. "And, as a company, we see a high rate of return."

Help juggle life demands. To help deal with the fast-paced and demanding environment at Starbucks, Working Solutions also provides referral services for partners and eligible dependents enrolled in the medical plan. It connects them with information that helps make extraordinary life issues more manageable. Moffat recently put the program to use when she needed elder-care advice for her grandmother. In another case, a partner needed emergency child care for his ill son. Working Solutions made prompt arrangements for a certified in-home caretaker, no work was missed, and Starbucks covered half of the cost.

Another example of Starbucks corporate caring: Three years ago, a Starbucks partner suggested a company-sponsored soccer team. The recommendation inspired *Partner Connection*, a program designed to link partners with similar interests, whether they be social, recreational, art and leisure, parenting or volunteerism. The Wonderful World of Food—a group that shares a common interest in great food and dining out—produced "The Partners Table," a cookbook whose sale benefits Fare Start (formerly Common Meals), a non-profit program that provides skills training to the homeless. A surge of interest in baseball resulted in a Starbucks softball league. Now, there's even a Starbucks choir. The New Parent Network, which offers such activities as CPR training for new parents, is especially active, given the significant number of Starbucks partners who are first-time parents.

Partner Connection is a program which links employees with similar interests, such as The New Parenting Network, above. This program ensures that Starbucks "partners" are happy outside of work, thus promoting satisfaction during work.

As part of the New Parenting Network, Anne Rauh, Starbucks administrative assistant for Learning and Partner Development, feels a special kinship with other Starbucks partners. "It's great to network on a consistent basis and share parenting issues with my colleagues," says Rauh. "Parenting isn't just something you do after 5 p.m., when you go home; you think about the things that are important to you—like your family—during the course of your workday. We're parents 24-hours a day."

The *Partner Connection* program, which requires little company cost, has flourished because the partners run it, and it stays responsive to their interests, company officials say. After partners were initially queried, it didn't take long for the program to gain popularity—almost immediately, 25 groups formed in Seattle. Similar partner programs operate throughout the company's regions.

Encourage a passionate partnership. As Starbucks pursues its coffee quest, the social and personal climate of the company continues to evolve. HR strives to stay abreast of its partners' needs and life-stages by periodically conducting opinion surveys. Its mission is to respond accordingly with effective work/life solutions. Starbucks provides onsite services that motivate a healthy mentality and allow for management of daily and extraordinary life demands. The company invites creative and innovative thinking through open communications, as well as established criteria for awards and recognition.

These elements, combined with a comprehensive benefits package, make for a passionate partnership between the company and its most vital resource. Being at the forefront among U.S. company benefits is central to Moffat. "We have the best and the brightest, and our success in the marketplace is directly related to our people," says Moffat. "We will ask our partners constantly what's important to them and consider these things as we plan into the year 2000 and beyond."

CEO Schultz had a mission since day one. "I wanted to establish the kind of company that gave people an opportunity for equity (ownership) and for comprehensive health insurance, among other things ... You can empower people with money and responsibility, but what about the person?" asks Schultz.

Starbucks answers that question. ■

Naomi Weiss is a freelance journalist based in Seattle, Washington. E-mail sunoob@workforcemag.com to comment

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[illegible] How do you maintain a sizzling hot growth rate without cheapening the brand? The problem starkly confronts Starbucks today.

The cappuccino conundrum

More star than bucks

Can food fuel more traffic?

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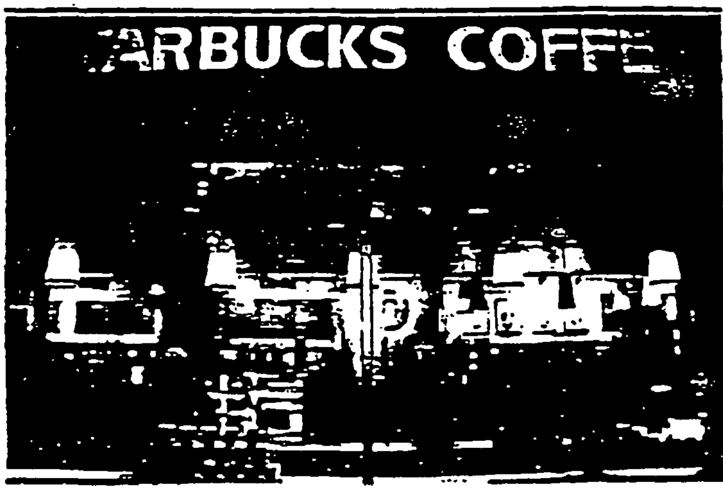
By Kelly Barron



HOWARD SCHULTZ IS A GENIUS. He discovered that if you translate "regular coffee" into Italian you can charge double for it.

Schultz hit on the idea of bringing the Italian espresso bar to America in 1983. Now his Starbucks chain is an institution, with 2,000 locations, including 170 abroad. Revenue in the fiscal year ending Sept. 30 will probably top $1.6 billion. With its progressive Seattle spirit—complete with stock-optioned counter crews—Starbucks created a new coffee cult. Wall Street values Starbucks Corp. at $4.7 billion, making Schultz, 45, worth $169 million.

But there are two things going wrong with this success story. One is that copycat stores are springing up on every other street corner. The other is that, even without a single competitor, Schultz would sooner or later run out of opportunities for expansion. And then what would happen to his earnings? Starbucks' average annual profit growth of 68% for the past four years is why its stock trades at a frothy 68 times earnings.

Growth at Starbucks' outlets is starting to slow. Store openings, occurring daily, propelled a 25% retail sales increase in the Dec. 27, 1998 quarter, to $343 million. But that's down from a 32% jump in the same period a year ago. What's more, sales at stores open a year or more grew at just 3% for the period, the lowest increase in seven quarters.

Starbucks alibis that same-store numbers are flattening because it purposely clusters units to saturate the market, thereby cannibalizing sales. Maybe. But in the restaurant business, unit profitability matters as much as ribbon cuttings. Every incremental dollar at an existing shop contributes 30 cents to 40 cents to the bottom line of a typical eatery. When same-store sales slow, it becomes more difficult to increase profits.

And so Starbucks is broadening beyond coffee shops. It partners with Dreyer's and Kraft Foods, putting its name on ice cream and coffee sold in supermarkets. It sells coffee to airlines. You also can find the brand stamped on bottled Frappuccino drinks, courtesy of a deal with PepsiCo.

What's wrong with this expansion? Just that it could conflict with the brand image. People pay up to $3.15 for a caffe latte because it's supposed to be a premium product. When you see the Starbucks name on what an airline is pouring, you wonder.

"Starbucks is losing its wholesomeness," grouses restaurant owner Hamid Moussavi, 38, as he sips his morning brew at a Coffee Bean & Tea Leaf cafe, across the street from a Starbucks in West Los Angeles.

The competitors, meanwhile, are going mass market, too. Pull up to a Mobil gas station and the convenience store has certified organic coffee supplied by Green Mountain Coffee Co. McDonald's pours a blend from Seattle Coffee Co. in the Pacific Northwest.

Growth has to come from somewhere. On the retail front, Starbucks is trying to increase its average sales ticket price—which a competitor says hasn't budged in nearly three years—by expanding its food offerings. That means everything from Krispy Kreme doughnuts in a New York City test to Fresh Fields gourmet sandwiches in Washington, D.C. It also is testing table service in Seattle at Cafe Starbucks, along with hot meals and alcohol. And in San Francisco it's going bohemian with Circadia—a coffeehouse concept with tattered rugs, high-speed Internet ports and live music.

Starbucks hopes more grub will draw traffic at lunch and dinner—when its cafes aren't as busy. But the introduction of food potentially complicates the simplicity and speed of Schultz's original concept.

"From a preference standpoint, Howard would probably not have to go into the mix he's entering," says Tom O'Keefe, chief executive of Seattle-based Tully's Coffee, a Starbucks competitor. (Schultz declined repeated requests to talk to FORBES.)

Another Starbucks venture: selling its Barista line of espresso machines and ceramic mugs in other retail chains. Maybe consumers will be more apt to

MORE

FORBES (concluded)
February 22, 1999

buy them at department stores than in the cafes, where merchandise sales stalled during December.

Then there's the recent acquisition of Tazo, a high-end tea company. Perhaps Schultz can create a constituency of tea snobs.

His larger challenge: to re-create an institution and keep it from going stale. That's a tall order—make that a *venti* order. Some companies have shrewdly managed to do so. The Gap went from selling jeans and T shirts to becoming America's most popular clothier, offering everything from men's suits to body lotion. Others, such as McDonald's, can't go far beyond burgers and fries.

If Starbucks is, in the end, the McDonald's of coffee, that's not the end of the world. Mickey D's stock trades at a hearty 36 times trailing earnings. But that kind of multiple would price Starbucks at $27—a long gulp down from its current $51. ■

Caffeine rush

The number of coffeehouses in the U.S. has grown from only 500 in 1991 to nearly 7,000 today, according to the National Coffee Association. Here's a look at the players trying to duplicate Starbucks' success.

[illegible]		
Second Cup Ltd	318*	Canadians operate Gloria Jean's, Coffee People, Coffee Plantation
[illegible]		
Seattle Coffee Co	72	Operates as Seattle's Best Coffee; often sells through others
[illegible]		
Peet's Coffee & Tea	44	Granddaddy of the industry; a favorite among the purists
[illegible]		

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Starbucks' CEO serves a blend of community, employee commitment

The story of **Starbucks Coffee Co.** may be rooted in the espresso bars of Europe, but the story of its chairman and chief executive, Howard Schultz, is distinctly American.

In what reads as the quintessential American Dream, Schultz left his working-class roots in the housing projects of Brooklyn, N.Y., to become the first member of his family to attend college, courtesy of a football scholarship to Northern Michigan University.

Upon graduation in 1975 with a degree in business, Schultz would embark on a series of career successes in sales and marketing with such companies as Xerox and the Hammarplast housewares. It was the latter position that introduced Schultz to a little coffee wholesaler in Seattle named Starbucks.

A year later Schultz would fulfill his own Manifest Destiny by venturing to the West Coast to work for that small coffee company. And by the age of 34 he would become its leader and begin building it into one of the most successful retail companies in America.

When Schultz came on board Starbucks in 1982, the company had five stores. Today it has more than 2,600 Starbucks outlets in North America and 15 international locations with annual revenues close to $2 billion and $100 million in profit.

Furthermore, according to Schultz, "when all is said and done, we'll have north of 20,000 units."

Starbucks opened 625 stores in the last 12 months, hires almost 700 new people a month, and serves more than 10 million customers a week, Schultz adds.

And that seems to be just the tip of the iceberg for this specialty-coffee juggernaut.

"One of the factors about the size and scale of the ultimate opportunity is that we have less than 5 percent of the market share in the United States, despite how successful we've been," Schultz says, adding, "and less than 1 percent on the world stage.

"The opportunity that we have to build a very big and sustainable enterprise is significant, and we believe we are in the very early stages of that strategic development."

In addition to building coffeehouses throughout the world, Starbucks increasingly can be found in grocery stores, airlines and other nontraditional locales. Then there's also the line of Starbucks ice cream and bottled beverages and an expanded cafe concept, Circadia, that serves a full menu and alcohol.

Moreover, in its effort to be everything to everyone, the coffee company sells its own "blend" of music and created its own magazine, Joe. On the new media front, Starbucks has partnerships with dot-com companies Oxygen Media and Talk City as well as its own, as-yet-to-be-determined Internet portal.

Also, in an ongoing commitment to community service and philanthropy, Starbucks has been involved in such high-profile programs as adult literacy, aided by baseball star Mark McGwire and Doonesbury creator Garry Trudeau, and has partnered with Earvin "Magic" Johnson's Development Corp. to open joint-venture units in urban areas.

Each venture has created a national buzz for the Starbucks brand name as much as for its coffee beans. As the company has grown in these various arenas, its name has taken on symbolic meaning.

"If you've got a Starbucks in your neighborhood, that's kind of like having the Good Housekeeping Seal of Approval — [it means] this is an OK place to do business," says Tom Lattimore of the Seattle Local Initiative Corp. "For these neighborhoods, they're an icon of change."

The success of Starbucks and its leader is threefold. It is the story of an organization committed to its people, committed to serving great coffee, and committed to maintaining an entrepreneurial spirit despite its highly scrutinized stock price.

In his 1997 book "Pour Your Heart Into It: How Starbucks Built a Company One Cup at a Time," Schultz began by telling the story of his father, who spent his life going from dead-end job to dead-end job without achieving any success.

Schultz wrote: "He had tried to fit into the system, but the system had crushed him. With low self-esteem, he had never been able to climb out of the hole and improve his life. The day he died he had no savings, no pension. More importantly, he had never attained fulfillment and dignity from work he found meaningful."

It is because of his father's legacy that Schultz has made Starbucks an organization based on respect and equality among all employees.

In his book Schultz wrote: "As a kid, I never had any idea that I would one day head a company. But I knew in my heart that if I was ever in a position where I could make a difference, I wouldn't leave people behind."

And today at Starbucks the high quality of life for its employees is as important as the high quality of its coffee.

Starbucks was among the first companies to offer health coverage to part-time employees and same-sex partners. It also was among the first companies to offer stock options to everyone in the entire organization.

"Treating employees benevolently shouldn't be viewed as an added cost that cuts into profits, but as a powerful energizer that can grow the enterprise into something far greater than one leader could envision," he wrote. "if people relate to the company they work for, if they form an emotional tie to it and buy into its dreams, they will pour their heart into making it better."

Those sentiments are echoed by those who work with him.

"Howard is first and foremost an exceptional human being. And I think you have to be a very exceptional human being to have the kind of values that he's imparted to the company," says Sharon Elliott, senior vice president of human resources. "He's very committed to enriching people's lives, and he is no less committed to doing that with the people who work for the company than he is in enriching the lives of the customers they service. That's it, that's the deal.

"If the person who is leading your company has those values, if those values are a seamless transition from home to work, and if that person has those very same expectations for the other people leading the company, then you're really going to have a great company and you're going to have a company that walks the talk of its values."

As a result of its strong benefits program and attitude toward all employees, Starbucks takes pride in having one of the lowest turnover rates in the industry.

"Our attrition is lower than anyone else in our peer group," Schultz says. "[That's] because people recognize us as a different kind of company.

"For me, without question, the reason we've been able to build a company this large is the culture and values of our company. Without the trust and confidence that exists because of that culture, we wouldn't be here. There are over 40,000 employees who we call partners because everyone is an owner," he says, proudly.

Yet, in addition to leading a people-focused organization, the story of Schultz and Starbucks is also about having a passion for the coffee business.

When Schultz met the founders of the original Starbucks in 1981, while he was still with Hammarplast, he immediately formed a bond with them when he saw how passionate. they were about the coffee business. Schultz wanted to be a part of what he believed to be an exciting opportunity to introduce Americans to specialty coffee.

"I was by his side when he decided to move to Seattle to work for **Starbucks Coffee Co.**," remembers Arthur Rubinfeld, a friend of Schultz's for 20 years who also heads up Starbucks' real-estate-development department. "Howard is a very passionate person who understood from the very beginning that the importance of his personal relationships at work and a passionate commitment to the work would enable him to be very successful. He had made a personal connection with the original founders of Starbucks, and that had motivated him to move across the country to start a new life."

It had taken more than a year for Schultz to be offered a job, despite his enthusiasm for the coffee business. Then in 1982 he moved to Seattle as Starbucks' vice president of marketing.

It was on a trip to Italy in 1983 to purchase coffee equipment that Schultz was introduced to the coffee bar.

Of the experience he wrote: "As I watched, I had a revelation: Starbucks had missed the point — completely missed it. This is so powerful, I thought. This is the link. The connection to the people who loved coffee did not have to take place only in their homes... What we had to do was unlock the romance and mystery of coffee, firsthand, in coffee bars. The Italians understood the personal relationship that people could have to coffee, its social aspect. I couldn't believe that Starbucks was in the coffee business, yet was overlooking so central on element of it."

But the owners of Starbucks weren't convinced.

While they finally acquiesced and allowed Schultz to open a small kiosk in the back of one of their stores to sell coffee by the cup, they would not expand the concept despite its popularity.

As a result, Schultz left Starbucks in 1985 and raised enough money to open his own coffee bar concept, Il Giornale. Soon the concept, which used Starbucks beans, grew to three units.

Meanwhile, the founders of Starbucks, who had earlier acquired San Francisco-based Peet's Coffee and Tea, a forerunner of specialty coffee in the United States, had decided to focus solely on the Peet's business. Back to Starbucks went Schultz, this time with the $3.8 million needed to buy the company.

In August 1987 Schultz was at the helm.

The company spent its early years focused on domestic growth, infrastructure and product development. In 1992 the company went public, raising about $29 million for expansion. A secondary offering in late 1994 netted approximately $180 million, ranking it among the better payoffs in foodservice history. Since going public, Starbucks has raised closed to $500 million.

Today, with a strong hold as the leading specialty-coffee retailer in the United States, Starbucks is focused on the international market.

"Five years ago our strategic intent was to build the leading brand of specialty coffee in North America. Five years later we have fulfilled that promise," Schultz says. "And our strategic objectives now are much different, and that is to maintain our leadership position in North America but to build an enduring global brand around the world.

"Also, I think more than anything else we now have demonstrated that Starbucks really has become the third place between home and work, and what we have created is not an American concept — it has universal appeal."

And as Starbucks continues to grow in unit counts, it also seems to be growing in new, alternative channels, including its expanded supermarket business and Internet presence. Schultz says it's all in the effort to maintain the ever-important entrepreneurial spirit of the company.

"I've always been a strong believer that you cannot embrace the status quo, and you need to keep pushing for reinvention. But that needs to be balanced with leveraging and executing at the highest level your core competency," he says. "But at the same time, being a merchant at heart, ifs incumbent upon us to continue to look for ways to do everything we possibly can to make sure that the Starbucks experience is differentiating in the marketplace, and that our customers